S. HRG. 98-883 PT. 1

HOW TO SAVE THE INTERNATIONAL TRADING SYSTEM

HEARING

BEFORE THE

SUBCOMMITTEE ON TRADE, PRODUCTIVITY, AND ECONOMIC GROWTH

OF THE

JOINT ECONOMIC COMMITTEE CONGRESS OF THE UNITED STATES

NINETY-EIGHTH CONGRESS

SECOND SESSION

PART 1

APRIL 26, 1984

Printed for the use of the Joint Economic Committee

U.S. GOVERNMENT PRINTING OFFICE

35-704 O WASHINGTON : 1984

J841-33

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(Created pursuant to sec. 5(a) of the Public Law 304, 79th Congress)

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CONTENTS

WITNESSES AND STATEMENTS

THURSDAY, APRIL 26, 1984

	Page
Roth, Hon. William V., Jr., chairman of the Subcommittee on Trade, Productivity, and Economic Growth: Opening statement	1
Yeutter, Clayton, president, Chicago Mercantile Exchange, former Assistant Secretary of Agriculture, and former Deputy U.S. Trade Representative	3
Bergsten, C. Fred, director, Institute for International Economics, and former Assistant Secretary of the Treasury for International Affairs	20
Hormats, Robert, vice president, Goldman, Sachs & Co., former Deputy U.S. Trade Representative, and former Assistant Secretary of State	23
Patterson, Gardner, former Deputy Director-General of the General Agreement on Tariffs and Trade (GATT)	26

SUBMISSIONS FOR THE RECORD

THURSDAY, APRIL 26, 1984

Gossage, Thomas L., group vice president and managing director, Monsanto International: Letter to Senator Roth concerning U.S. policy toward the international trading system, dated May 30, 1984	52
Yeutter, Clayton: Address by Arthur Dunkel, Director-General of the General Agreement on Tariffs and Trade, before the 47th Chicago World Trade Conference, April 24, 1984	5

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THURSDAY, APRIL 26, 1984

CONGRESS OF THE UNITED STATES,
SUBCOMMITTEE ON TRADE, PRODUCTIVITY,
AND ECONOMIC GROWTH
OF THE JOINT ECONOMIC COMMITTEE,
Washington, DC.

The committee met, pursuant to notice, at 10 a.m., in room SD-342, Dirksen Senate Office Building, Hon. William V. Roth. Jr. (chairman of the subcommittee), presiding.

Present: Senators Roth, Mattingly, and Bradley; and Representative Holt.

Also present: Charles H. Bradford, acting executive director; and Ruth Kurtz, Sandra Masur, Dale Jahr, and Robert R. Davis; professional staff members.

OPENING STATEMENT OF SENATOR ROTH, CHAIRMAN

Senator ROTH. The subcommittee will be in order.

I want to say at the outset that I have been looking forward very much to the discussion we are going to have today and I particularly want to thank those of you on the other side of the table for being here with us.

I think we are very fortunate in having such an outstanding group of experts who have provided strong leadership in trade in the past and certainly will continue to do so in the future.

None of them really need any introduction, but I am delighted to have here today Fred Bergsten, who was under President Carter Assistant Secretary of the Treasury. Most importantly, he is one of the intellectual thinkers of our community. Mr. Bergsten, we are delighted to have you stop here for all those reasons.

Bob Hormats, the last time we were together was over in Brussels where we were addressing the European Community. Mr. Hormats, you provided strong leadership both as Assistant Secretary of State, and as Deputy U.S. Trade Representative and we are delighted to have you here.

Then we have Gardner Patterson, who will bring some insights that I think are indeed needed. He is former Deputy Director-General of GATT.

Finally, I come to you, Clayton Yeutter. Mr. Yeutter, has played so many key roles, including being present head of the Chicago

Mercantile Exchange, and also a former Assistant Secretary of Agriculture and a former Deputy U.S. Trade Representative.

So I want to extend a warm welcome to each and everyone of you. We thought we would experiment a little bit and change the approach to hearings. We Members of Congress like to sit up there on the bench and ask difficult questions that we cannot answer. What I am hopeful of is that this discussion today will be very free flowing with everyone free to ask questions of others or break in at appropriate moments. I did think we would start out with brief comments, hopefully kept to 5 minutes on the part of each one, and perhaps we should not intrude on those so that each person has a chance to make whatever statement he cares to. I would say that I would hope that we would avoid at least any lengthy discussions on some aspects of the problem—the deficit, the exchange rates the problem of slow recovery on the part of other regions of the world.

What I would like to dwell on today is the long-term issue of the international trading system itself. The theme of this hearing is how to save the international trading system. This may sound alarmist, but I think perhaps it is time to sound the alarms.

Ostensibly, world trade and U.S. trade interests are protected by GATT, the postwar answer to the destructive trade policies of the 1930's during the so-called Great Depression. Today 88 nations, accounting for four-fifths of world trade, are members of the GATT. That sounds very good and very encouraging, but this membership hardly reflects a growing commitment to today's traders to the basic principles and premises of the GATT. While GATT membership has grown for 23 to 88 countries, the agreement's principles and premises have become increasingly irrelevant to the real trading situation.

Let me just cite one example. The GATT and U.S. support for it is grounded in a free market philosophy. The GATT rules presume that trade is primarily conducted by private actors in markets in which prices are set by a free interplay of supply and demand.

This is far from the situation today. European governments now have a direct ownership stake in over half of Europe's 50 largest companies, and in some countries state-owned companies amount to nearly half of the industrial sector. In other countries—Japan, probably the most noted example—the state may not own the productive facilities, but it does play a significant role through industrial policy, especially for targeted industrial sectors.

So frankly, it is no wonder that the frustrations of this increasingly uneven competitive environment have led many to call for the protectionist or unilateral responses to even the playing field.

But I believe that protectionist responses are mistaken because they misunderstand the long-term U.S. trade interests. Protectionism might make trade fair in this country, but the cost will be high in lost export sales as other countries retaliate against us. And of course, domestic protectionist actions will do nothing to make trade competition fairer in international markets, the real future for U.S. jobs and economic growth. I, for one, believe that we shall see great strength and great growth in the world economy, particularly in the Pacific Basin, but elsewhere, and that it would be a serious mistake if we do not adopt policies to participate in this growth.

Perhaps this confusion results because the current somewhat catchy phrase that we like to use to describe our basic trade objectives—free and fair trade—is, at best, too obscure. At worst, I believe it is a code for protectionism. We can start creating a U.S. trade policy for the 1980's and 1990's by adopting a new phrase to capsulize U.S. trade objectives: Instead of free and fair trade, let us talk about equitable and expanding trade.

When we clearly recognize that we have two trade objectives—to make trade equitable and to help it expand—it also becomes clear that we must find better ways than protectionism to pursue our duel trade interests.

So that is what this so-called hearing is all about.

The basic question I would like to pose to both the distinguished witnesses and my distinguished colleagues today is, how can the international trading system be reformed to bring equity to our trade relations and at the same time support trade expansion?

Now for any and all the historians we may have in the audience—they look pretty young to be historians to me—I would point out that this discussion takes place in the 50th anniversary year of the Reciprocal Trade Agreements of 1934. With that act, this country turned its back on the isolationist policies of the Great Depression, and provided the President with the authority to lead a worldwide movement for reduction of tariffs and other barriers to trade from which the GATT grew. At this 50-year juncture, it would seem to me to be a particularly good time to take another look at U.S. policy toward the international trading system.

So again, I welcome the members of the panel as well as those sitting out in the audience.

Senator Mattingly, do you care to make any remarks?

Senator MATTINGLY. Not at this time, thank you.

Senator ROTH. Congresswoman Holt.

Representative HOLT. I have no comments. I welcome our guests today. I am looking forward to your comments. Thank you, Mr. Chairman.

Senator ROTH. Who would like to lead the panel? Mr. Yeutter, how about you?

STATEMENT OF CLAYTON YEUTTER, PRESIDENT, CHICAGO MERCANTILE EXCHANGE, FORMER ASSISTANT SECRETARY OF AGRICULTURE, AND FORMER DEPUTY U.S. TRADE REPRESENTATIVE

Mr. YEUTTER. Thank you, Mr. Chairman.

First of all, I want to commend you and your panel for having this kind of hearing. It is precedent setting because typically we concentrate on the issues from a short-term viewpoint and rarely does anybody look at the big picture or the long-term picture, and certainly that is in order at this time.

I just came in this morning, Senator Roth, from having been involved in Chicago's World Trade Conference. We have an annual conference in our city which is the largest trade conference in the United States. Ambassador Brock was on the program yesterday; and Arthur Dunkel, Director-General of GATT, the night before;

the Canadian Trade Minister, Mr. Regan, at noon; and a lot of other country representatives. It was a superb conference.

But one of the points that Arthur Dunkel made in his address Tuesday night was that he felt that the international trading system was at a crossroads. Certainly if the Director-General of the GATT feels that way, that makes this kind of hearing become timely and appropriate.

Incidentally, Mr. Chairman, I brought along a copy of Director-General Dunkel's address delivered before the 47th Chicago World Trade Conference on April 24, 1984, which I thought was outstanding. I would like to leave one with you and if you wish to insert it in the record of this proceeding, please feel free to do so.

Senator ROTH. Without objection, it will be placed in the record at this point.

[The address referred to follows:]

ADDRESS BY ARTHUR DUNKEL, DIRECTOR-GENERAL OF THE GENERAL AGREEMENT ON TARIFFS AND TRADE, DELIVERED BEFORE THE 47TH CHICAGO WORLD TRADE CONFERENCE, APRIL 24, 1984

1. It is a great pleasure for me to be for the first time in Chicago, a city where the free trade philosophy has always been so powerful. I hope it still is powerful, and not just in theory, because this conference is taking place at a turning point in the history of the world trading system. As so often in the past, the United States is in a pivotal position; a great deal depends on the direction taken by US trade policy, whether towards or away from multilateral free trade principles, and on the response to it elsewhere.

2. I usually dislike starting a speech by quoting statistics. This distaste has grown over the last two or three years, when it seemed that virtually every speech and article about world trade began with gloomy references to its stagnation in 1981 and its decline in 1982. Tonight, however, I do want to spend a few minutes on the trade figures which will shortly be published in the Annual Report of the GATT. They are revealing because on one side they give welcome evidence of the reality of economic recovery but on the other they also show why the recovery in itself will not relieve governments of the need to confront the structural problems which the recession exposed so brutally.

3. The fact that the volume of world trade increased by 2 per cent in 1983 is in itself nothing to write home about; it merely means that by the end of the year trade had recovered to its 1980 level. What is more significant is that its rate of growth was much faster in the second half of 1983 and seems still to be

increasing. Even if there were no further acceleration - if trade stabilised at its current level - 1984 would show a 4 or 5 per cent increase over 1983, and there is good reason to expect better than that. Most forecasts suggest that economic growth in the industrialised world, and notably in Europe, will be substantially faster this year than last.

4. The recovery of the world economy from the deepest recession since the 1930s is therefore under way. But it has so far taken place on a disturbingly narrow base: the figures show that one-half of the net growth in world trade in 1983 was accounted for by the increase of exports to the United States. While this demonstrates very clearly the vital rôle of the US as the leader of the recovery, it is one of the factors behind the mounting trade deficit which magnifies the protectionist pressures to which the Administration is now being subjected. These are, I hope, a short-term problem, since the recovery is spreading to the major export markets of the US, but it is a serious one. Behind it there lie the structural problems, still unsolved, which helped to deepen the recession.

5. Let me take the short term first. It can certainly be argued that by maintaining a trade deficit at its present record level - I understand it is running at an annual rate of about 117 billion dollars - the US is doing far more to stimulate growth elsewhere than could be done in the short term by trade policy measures. I recognise the truth of that. Indeed, I remember Malcolm Baldridge, as long ago as January 1982, predicting these massive deficits, which he said the United States would accept, despite the political problems they would cause, as its contribution to world recovery.

That is a pledge which has been kept, in that the Administration has resisted whatever temptations there might have been to reduce the trade deficit by an across-the-board restriction on imports. One has only to contemplate the likely effects of a 1971-style import surcharge, or any comparable measure, on the world recovery to appreciate how vital this resistance has been, and will continue to be.

6. Therefore, notwithstanding some over-simplified reports of a speech which I made in London in February, I do not accuse the US Government of protectionism. Restrictive measures have been taken, and I shall return to those in a moment, but what worries me far more is the mounting pressure on the Administration, not just for protection of a long list of industries but also for legislative changes which would imply a retreat from the US commitment to the principle of multilateralism.

7. I have in mind some of the bills now before Congress - those on bilateral reciprocity in trade and on the domestic content of imported automobiles, and the Wine Equity Bill. All of these give expression to a belief - or at least a claim - that the open trading system is somehow biassed against the United States and that the way to make it fair is to exact bilateral reciprocity from each of her trading partners.

8. The Wine Equity Bill is an extreme case, because it would impose, as a new guiding principle in international trade, bilateral reciprocity in a specific and narrow sector. It would run completely contrary to the principles on which the reduction of

tariffs has been negotiated in the GATT for the last thirty-five years; precisely because negotiators have been able to balance tariff reductions given in one sector against those received in another, and because these reductions have been applied on an m.f.n. basis, it has been possible to reduce the average tariffs applied by industrialised countries to negligible levels. This has had enormously beneficial results for the world as a whole.

9. Strict reciprocity of the kind envisaged in this bill would be likely to restore protection to pre-war levels and destroy the multilateral system. If I may say so, I think that the Administration was very wise to request Congress not to pass this bill. It was also profoundly encouraging to read of the vigorous and forthright testimony, in opposition to protectionist legislation, recently given before the Senate Finance Committee by Bill Brock and other senior representatives of the Administration. There is no need for me to point out the malign effect of the present level of the dollar on the US trade deficit, when Bill Brock and others have done it so clearly and have thereby demonstrated the irrelevance and danger of trade restriction as a remedy for the payments deficit.

10. To some extent, no doubt, the upsurge in protectionist pressures is a temporary phenomenon, associated with the trade deficit. I hope it can be expected to subside next year, particularly if America's export markets are then booming. But if the problem is more fundamental - if it masks a reluctance to adjust to changing market conditions, caused by erosion of US belief in and understanding of the open market system - then we are all, not least the US itself, in serious trouble.

11. Starting from the wartime negotiation between the United States and the United Kingdom of the agreements on which the basic rules of the GATT and the International Monetary Fund were based, right up to the initiation of the Kennedy and Tokyo Rounds, the US has played a leading rôle at every stage of the GATT's development. I have always understood that insistence on multilateralism and on the rule of law in trade relations were basic principles of US policy. They are as valid now as they ever were, but they are under constant challenge: first by those who have lost faith in their ability to adjust and compete in an open trading system; and secondly, through "temporary" and illegal bilateral deals, by some who claim to have the best interests of the GATT at heart. To restore the American consensus in favour of free trade principles is absolutely essential. To put it starkly, the trading system based on GATT rules cannot survive without the whole-hearted commitment of the United States, and the United States cannot prosper without the system.

12. I am not arguing that the trading system is working well and that the United States or any other contracting party should be content with it. In many respects it needs strengthening and reform, and like all contracting parties the US has some legitimate complaints.

13. Many difficulties can of course be resolved in the normal course of the GATT's work. Let me mention three examples, the US complaint about the trade effects of the Canadian Foreign Investment Review Act was settled, satisfactorily from the US point of view, by a GATT panel finding that a requirement that foreign

investors in Canada should undertake to buy Canadian goods was inconsistent with the GATT. The report has been adopted and Canada has undertaken to bring FIRA operations into consistency with its GATT obligations. The reform of Japanese standards and certification procedures was spurred, accordingly to the Japanese themselves, by the GATT Standards Code. The Committee which administers the Agreement on Trade in Civil Aircraft has recently recommended the abolition of duties on thirty-two new product categories.

14. But it would be idle to pretend that the problems rooted in deeply entrenched national policies which underlie such issues as subsidies and agriculture could be resolved in the same way: the international law is too ambiguous and the political stakes too great. I understand and sympathise with the view that the Subsidies Code negotiated in the Tokyo Round is not working well. I regard the growing distortion of competition (in the industrial as well as agricultural sectors) through subsidies as one of the most pernicious forms of protectionism. Related to this is the sense of grievance which the US shares with other traditional agricultural exporters about the application of GATT rules to agricultural trade. The question is, how can these long-standing problems, and those which preoccupy other contracting parties, be resolved?

15. So how do we deal with these problems? Since we are in Chicago, let me take agriculture, which involves some of the biggest structural problems as well as being at the root of some of the short-term pressures I mentioned earlier: [In] Agricultural [redacted] access to markets is highly restricted, the conditions of competition in

third markets have degenerated and governments everywhere are concerned by the explosion of the direct and indirect costs of support and protection for domestic production. Subsidised production and domestic price supports have led first to the reduction of access for imports, then to massive structural surpluses which are unloaded onto world markets with the help of further subsidies, causing severe disruption of the market function and - let us not forget - the atrophy of domestic agriculture in many developing countries. We have seen direct competition between the Community and the US by means of subsidised exports to developing countries. Even the attempts which are now being made to contain the problem can create further tensions. One result of the Community's struggle to limit its own production surpluses and budgetary deficits is the recent decision to stabilise imports of corn gluten by establishing a tariff quota.

16. All this has happened despite GATT rules which, though they include some special provisions for agriculture, nevertheless make it clear that any restriction of agricultural imports should be accompanied by effective internal production controls and the maintenance of the traditional relationship between imports and domestic production. Why have they been so widely evaded? One reason, I fear, is that the US itself was unable to live with these provisions (or with a proposed ban on export subsidies on agricultural and other primary products) and in 1955 sought the waiver from certain GATT obligations which has protected US agriculture ever since. The waiver pre-dated by a few years the elaboration of the Common Agricultural Policy, and it set a

precedent for differential treatment which the Community, Japan and others - including Switzerland, which secured special protection for agriculture in its Protocol of Accession to the GATT - were not slow to follow.

17. A chance now exists, perhaps the first since 1955, to make GATT rules fully operational in agriculture. Governments are being forced to reconsider the economic and political logic of post-war protectionism. In 1984 the Community will spend 16 billion dollars, and the individual member states as much again, on farm support, and last year in the US the direct costs alone were 22 billion dollars.

18. It is no coincidence that if the political incentive to cooperate now exists, so does the necessary international machinery. One of the most positive results of the Ministerial meeting held in GATT in 1982 - which was by no means an unqualified success in all respects - was the creation of an Agriculture Committee with a mandate to examine all protection and support policies, including domestic support, and recommend ways of liberalising agricultural trade. Somewhat to the surprise of old hands who have seen earlier attempts founder for lack of goodwill and political commitment, the Committee is working well. There is general agreement that the rules relating to agriculture have not been applied with sufficient rigour and that the rules themselves can be improved. If it is to be done, however, leadership from the major participants, based on recognition of their common interest in finding a rational solution, will be essential.

19. Mention of common interests reminds me, perhaps rather late in the day, of the theme of this conference. Because I do not agree with what I take to be its implications, I found the title "World Trade - Objectives in Conflict" provocative and stimulating. It seems to me that the great problem in world trade at the moment is not that national objectives conflict, but that they are ill-defined, and that we have got into a dangerous habit of adopting adversary positions almost automatically. Take the example of North-South relations, which have been bedevilled by a false picture of two great blocs whose interests are necessarily in conflict. Could the reality of the interdependence between them have been demonstrated more convincingly than it has been by the debt crisis? The recession we have just lived through would be as nothing compared with the consequences of collapse of the financial system.

20. On a more mundane level, it is clear that the contraction of imports into the heavily indebted countries - and into the traditional oil exporters - severely affected the export performance of industrialised countries last year - though less that of Japan than of the North American and European countries. It would be preferable from every point of view, particularly that of the indebted countries themselves, if their payments adjustment could take place through export expansion, but for this they depend on economic growth and open trade policies in the developed world. I believe the growth is there, but what of the trade policies? What signals have been given to potential investors in Latin (and other developing countries) America by developments in US textiles policy? What scope would be left by the worldwide cartelisation of the steel industry for (and other industrial countries)

and other developing countries/

expansion of the steel exports of Brazil, even if the problem of subsidies had not arisen? I know that Brazil is running a large trade surplus with the US. I know that the USA, the Federal Republic of Germany, the United Kingdom and Canada between them take in 75 per cent of the developing countries' exports of manufactures to the developed world, and that the growth in these markets has greatly benefitted the developing countries of the Far East, in particular. But which stories get the headlines?

21. I think many people in the US, and indeed elsewhere, see relations with the developing countries as one of the structural problems of the GATT, in the sense that the status of developing countries is undefined and the special rules applying to them make no distinction between the different levels of development within the group. It is sometimes suggested that there should be graduation (let us not be afraid of the word) by countries attaining the higher levels of development through the acceptance of more of the obligations of GATT membership. The concept is not popular, but I am not sure that all developing countries would reject it out of hand. Some of them might be fully prepared to accept the same obligations as developed contracting parties if that meant that in return they would receive the same treatment - for example, no quantitative restrictions on their exports of textiles, clothing and agricultural products and no pressure for "voluntary export restraints" in other sectors where they have attained competitive efficiency.

22. This brings me back to the question I left hanging at the start of this speech. For years we in the GATT have been expressing the fear that trade protection and other distortions of the market mechanism would weaken and slow down the spread of economic recovery. I hope that 1984 and 1985 will prove us to have been wrong, but the patchy and sluggish response last year of most other economies to the powerful stimulus of US demand gives point to a question on which governments will have to focus in the next few months: are there impediments, whether economic, administrative or psychological, to the spread of recovery and the achievement of stable growth which it is now within the power of governments to remove, unilaterally or in cooperation? If there are, the interest of every trading nation in consolidating this recovery demands that the necessary action be taken.

23. By their agreement at the Williamsburg Summit last summer, the leaders of the seven major industrialised powers not only recognised that it was possible to roll back protectionism: they pledged themselves to start the process. So far the pledge has not borne fruit. Nobody now disputes, however, that there are fundamental problems which have to be settled before they destroy the trading system, and that there is not very much time left. This is why a number of governments, with Japan and the USA, among others, taking a very positive position, have called for the start of another major round of trade negotiations in the GATT: if there is a complex of interrelated problems to be solved, it may well be easier to take them as a package rather than piecemeal.

24. As Director-General of the GATT I can only welcome a renewed cooperative effort; I believe in the technique and I know there is useful work to be done. Nevertheless, some other governments approach the idea with a good deal of caution, and one can see why. A new round could resolve many difficulties, but it could also, if it fails, defer their resolution indefinitely. Nor should the prospect of a new round be allowed to delay progress on those issues where it is possible to move forward in the short term. Finally, a new round could only succeed if a sufficiently large number of countries are persuaded that overall its results will benefit them. The USA has made very clear, as it is fully entitled to do, its desire that the negotiations cover effectively new areas of services, investment and high technology; but many other contracting parties have relatively little interest in these areas and need to be satisfied that progress is to be expected on the questions of most concern to them. To achieve consensus on the agenda and objectives of any negotiation is therefore a first priority. But a premature or ill-prepared initiative would do more harm than good.

25. If I were a member of a national adminstration trying to judge whether I should lend the concept of a major new round my support, I think I should put to myself five questions:

- Is it likely to help us find a rational way to take account of the special needs of developing countries, while integrating them more fully in the GATT system, as partners rather than recipients of differential treatment and simultaneously as objects of discriminatory restrictions?

- Is it likely to put an end to the proliferation of protective measures taken outside GATT rules and subject to no multilateral disciplines?

- Will it help to bring agricultural policies, including domestic policies where they affect international trade more nearly into line with the principles of competition and comparative advantage?

- Will it help to reverse the dangerous escalation of competition from subsidies?

- Will it, in overall terms, strengthen the GATT system as a basis for secure and predictable trade relations for the rest of this century?

26. There is no reason in principle why the answers to all these questions should not be positive, but this could only be so if there were a real sense of common commitment - an understanding that international trade is not a zero-sum game, in which one country's advantage can only be secured at the expense of another. I hope this conference will have helped to create such an understanding.

Mr. YEUTTER. Getting to the subject at hand, there are a lot of things we could concentrate on this morning, of course, and I would like to just articulate a few which seem to me from my viewpoint in the private sector to be especially critical. We can expand on these and embellish upon them during the proceedings.

First of all, starting from my background as an agriculturist, I would say that a major shortcoming of the GATT is its failure to effectively confront agricultural trade issues. For all practical purposes, the GATT does not even affect agricultural trade. Essentially, the major trading nations of the world do what they wish in agricultural trade. There are essentially no real rules of the game in that area. Considering the magnitude of agricultural trade and the growth potential it has in many countries—and particularly the importance of agricultural trade to this country—the situation obviously merits considerable attention.

As you know, in the last GATT Ministerial, an agriculture committee was formed to begin to do some creative thinking in this area. Apparently it has gotten off to a reasonably good rhetorical start, but nothing has yet been done on the rules.

I happen to think, Mr. Chairman, that the timing is propitious for confronting that issue now. Even the European Community has begun to realize that what is happening in agricultural trade and in agricultural policy just cannot go on. I read a speech on this issue just a day or two ago by Claude Villain, Director-General for Agriculture of the European Community. It was the most reasoned, balanced presentation on agricultural trade I have ever seen coming from a representative of the European Community.

That says to me that the time is ripe to deal with agricultural issues in a more decisive way in the GATT.

My second point relates to the question of export subsidies. Director-General Dunkel concentrated on that issue at some length in Chicago a couple days ago. He pointed out—and I certainly agree with him—that the subsidy code negotiated in the Tokyo round simply is not working well. That may be an understatement. Some of us might suggest it is not working at all. It may be somewhat better than not having a code at all, but not much.

So something has to be done in the export subsidy arena. That is perhaps more important in agriculture than in other areas, but it is clearly becoming a factor in nonagricultural, industrial trade as well.

One of the other issues that the Director-General brought up as being of concern to him as head of the GATT is the increased bilateralism and the shift away from multilateral treatment of trade issues. I share this concern. In fact, I suppose the United States may be as guilty as anyone of practicing bilateralism. Some bilateralism is inevitable, but certainly the Director-General aptly points out that if we move more and more down the road to bilateralism, one must wonder what the role of the GATT can be—with the basic multilateral orientation that it has had from the very beginning.

Another issue that we ought to talk about a bit this morning, Mr. Chairman, is the relationship of the developed world to the developing world in the GATT. That question has not been handled well either. We started during my years in Government with what

was then called "special and differentiated treatment" for the lesser developed nations. That has had mixed blessings. It is not a very satisfactory relationship from the standpoint of the developed countries, like the United States, and it has not been very satisfactory from the standpoint of the lesser developed nations either.

Nor have we done a very good job of bringing the developing nations in as members of the GATT. Mexico, as you know, deliberated long and hard on this question a few years ago and finally decided not to join. Well, it seems to me that if the developing world wishes to take advantage of the privileges of GATT, then it ought also to have some of the responsibilities of the GATT. One of the responsibilities should be to function as members and not sit on the outside.

It also seems to me that the GATT soon must confront that question, if for no other reason than that UNCTAD would love to become the international trade guru of the world, a result that is not likely to be in the interest of the United States. We would function about as effectively in UNCTAD as we do in the United Nations as a whole—not very well indeed.

So if we are to avoid having that agency take over an increasing level of responsibility in the arena of international trade, the GATT must do its job well, properly balancing interests between the developed and the lesser developed countries.

I have to mention dispute settlement, too, from the perspective of the private sector. The GATT has for years wrestled with the question of dispute handling. It has never done this very successfully, which is perhaps inevitable, because it is difficult for any international entity to resolve disputes between and among countries. A lot of nationalism is involved, and no nation wants to surrender a portion of its sovereignty in a dispute settlement process.

But at the very least we could insist that the GATT be more decisive, reaching conclusions much more quickly than it does. Whether it settles the dispute or not is another question; but the GATT ought to be able to quickly decide questions such as: Is a practice in violation of the principles of international trade or not; does it violate a GATT article or does it not; or does it violate the spirit of the article, if not the letter?

As you will recall, Mr. Chairman, we had that same problem in U.S. law for a long time, with our Government being unresponsive to the private sector, dragging out decisions for years and years. You and your colleagues changed that a few years back by requiring definitive timetables for decisions by the U.S. Government. In my judgment, that has been very, very helpful; we need to move a lot closer to that in the GATT framework.

My final comment relates to safeguards. Clearly, safeguards are an important segment or element of the protectionism question, the whole matter of when a nation can properly protect its industries from being inundated by exports from other nations.

We were working on the proposed safeguards code when I was in Government almost 10 years ago, Senator Roth. That was during the Tokyo round. Unfortunately, the issue was not negotiated satisfactorily; we did not emerge from the Tokyo round with a safeguards code. This is a horrendous omission from the rules of international trade, and one of the highest GATT priorities should be to

bring a safeguards code to fruition. At the moment, we are not making any visible progress that I can see.

In closing, I would like to repeat a comment by Director-General Dunkel from his presentation in Chicago. Our conference in Chicago related to trade objectives being in conflict around the world. Director-General Dunkel said he was not really taking issue with that, but he thought it was not so much a matter that objectives of the major trading nations were in conflict, but that their objectives were ill defined. He added that the GATT is what the major trading nations of the world want it to be, but in his judgment, the major trading nations of the world do not know what they want it to be. Until the United States and other countries begin to define what their objectives are for the GATT and for the international trading system, it will continue to be very difficult to accomplish very much, according to Mr. Dunkel.

It is obviously a question of leadership and a question of commitment on the part of the major trading nations. Thank you.

Senator ROTH. Let me just make a couple of comments and then I will turn to you, Mr. Bergsten.

First of all, using the terms equitable and expanding, I would hope that that would be something that would have some appeal to everyone because it seems to me that it is in everybody's basic interest.

As a member of the Finance Committee, I remember when we were authorizing the new negotiations. One of the key purposes of the multilateral trade negotiations, of course, was to try to break down the agricultural trade barriers. Unfortunately our negotiators found that if they wanted to make any progress whatsoever that they had to yield on that. So I think it is very encouraging to hear you say today that you think the situation is ripe for negotiations in this area.

I mentioned that Bob and myself were over in Brussels and one of the things I discussed there was the European Community's outmoded policies. They are protecting an industry, if you want to call agriculture an industry, that is not competitive and they are losing out. They are declining, as was so eloquently brought out in Newsweek. So I think it shows very well why agriculture trade should be opened and why it is in their interest as well as ours.

Fred, I would like to call on you next for comments you may have.

STATEMENT OF C. FRED BERGSTEN, DIRECTOR, INSTITUTE FOR INTERNATIONAL ECONOMICS, AND FORMER ASSISTANT SECRETARY OF THE TREASURY FOR INTERNATIONAL AFFAIRS

Mr. BERGSTEN. Thank you very much, Mr. Chairman.

Let me first echo Mr. Yeutter's praise for you in having these hearings, for two reasons. When you entitle them, "How to save the international trading system," I think you have it just right. My view is we are now facing the greatest threat to the international trading system literally in 50 years, since the advent of that period you mentioned that started in 1934. So I think you had better have hearings on this and consider these questions seriously.

Second, the strategic steps that I am going to suggest for saving the system all go in very important part right here to the U.S. Congress and suggest actions that need to be taken in this body to help save the trading system. Not that you can do it by yourselves, but all of the steps do go directly to requirements for action here. I think, again, it is particularly appropriate that you have these hearings.

As I mentioned, I think there are three basic areas in which strategic steps are needed if we are going to save the system.

The first of those is outside the trade system per se, as normally thought of, and has to do with the exchange rate and international monetary matters. I take your admonition, so I will not dwell on that at length, but I want to assert the following very strongly: the United States will face neither equitable trading opportunities nor expanding markets until it gets the exchange rate for the dollar right. The dollar is now at least 25 percent overvalued in terms of the underlying competitive position of our producers. That means we are putting a tax of 25 percent on everything we try to sell abroad. It means we are paying a subsidy of 25 percent on all imports coming into this country. As long as that happens, you do not have the preconditions for an open trading system in either intellectual or policy terms.

The trade deficit this year will hit at least $120 billion, next year it will hit on my reckoning about $150 billion, and it is continuing to rise, not because of an underlying lack of competitiveness on the part of our industries and workers, but because they are priced out by the overvalued dollar in the exchange markets.

I will not dwell on it, but I will simply suggest two things. Getting the exchange rates and the monetary system right will not solve all of our trading problems, and therefore the things that Clayton and others are referring to in these hearings are clearly critical, but I think that unless we get the monetary issue correct, you will not be able to save the trading system whatever else you do. I think it is a necessary condition and that means taking steps to get the dollar-exchange rate right now. It also means taking steps to change the international monetary system in a way but will prevent huge imbalances of this type developing over the future. That is all I will say on it for now. We can talk about it later if you want details, but I really would put that at the top of my list and urge that those of you who work directly on trade and the trading systems not simply leave the monetary side to the financial types because that has been done for too long and the result is failure.

Second, I think particularly you in the Congress, but working with the administration, are going to have to develop a new program of domestic adjustment within the United States to trade-generated dislocation for American industry and workers.

For the last 20 years, from the early 1960's to the early 1980's, we did have a program of trade adjustment assistance. It was by no means perfect either in concept or in practice. Nevertheless, it did provide an alternative in both economic and political terms to the application of trade restrictions as a response to legitimate problems that industries and workers faced from competition from

abroad. That program has been almost totally gutted over the last 3 years.

Again, I would think it is unlikely that we will be able to save the trading system unless the United States, the central country in the trading system, not only gets the exchange rates right and gets the monetary relationships corrected, but puts back in place some kind of domestic adjustment mechanism to provide an alternative to trade controls for industries which have legitimate problems with foreign competition. Otherwise, you will not have any alternative in a political or economic sense to putting up new barriers.

Those problems, both the exchange rate and domestic adjustment, are critical and the Congress may have to take the lead on them.

The third strategic point encompasses all of the specifics that Clayton mentioned but a lot of others as well. It seems to me strategically essential to move as rapidly as possible to launch a major new international trade negotiation.

I happen to be a strong advocate of something that has come to be called the bicycle theory, which suggests that trade policy either moves forward toward greater liberalization and expanding trade, as you put it, or else topples on its side and gives way to particularistic pressures for protection in individual sectors.

The history of trade policy, certainly throughout the postwar period, gives strong support to that approach and suggests that we must move as quickly as possible into a negotiating mode of that type.

Policy interdependence is enormous today, as you suggested in your own comments. What Japan, Europe, and the developing countries do feeds back on what we can do or would want to do here with our trade policy, and only if all those major trading groups are moving together in an expanding direction can any one of them move on its own in an expanding direction. So it is essential to mobilize, both in terms of our internal politics and then internationally with the other major trading countries, to move in a trade-liberalizing direction, to deal with many of the old problems—agriculture, safeguards, subsidies that Clayton referred to quite rightly—in addition to a number of new problems.

My Institute for International Economics published a study on this topic a little over a year ago called "Trade Policy in the 1980's," based on extensive analysis and a major conference, in which we tried to lay out what the component issues in a negotiation of that type would be. I think it provides at least one basis for the possibility of moving ahead in that direction today.

So I would say at the level of strategy, saving the trading system, we are going to have to make major changes in the monetary relationships both now and for the future. We are going to have to put in place a new domestic adjustment system in this country and we are going to need to move toward a new multilateral trade liberalizing and moving negotiation as soon as possible.

Senator ROTH. Thank you, Mr. Bergsten. Let me just point out that I agree with you as to the importance of monetary policy and it may be that this group ought to have a hearing on that explicitly because I always get lost during the discussion but it is something that has to be faced. In any event, one of my concerns we have

talked about this many times at your initiative, Fred—is that there is no coordination between monetary, trade, and fiscal policies domestically, and I think the same thing is true internationally with the World Bank, the IMF, the GATT, and so forth.

I think it would be the height of folly to try to form some new powerful organization to coordinate trade and finance. I just do not think that is doable or maybe it is not even desirable. But in any event, I do think some coordinating, consulting basis might be in order, and I think that is something we would like to explore further with you.

Let me just make one comment, as one who several years ago saved the adjustment program on the Senate side and tried to modify it, one of the concerns—and it is a legitimate concern—is the cost of any major program and how do you finance it?

I would be interested—would it be appropriate or proper to try to work out in some kind of negotiation, some kind of a small charge that might be made on trade as a means of financing these adjustments, not as a barrier but as an expediter of trade expansion? I think that might be worthwhile exploring a little.

I would like to turn to Mr. Hormats because, as I said, I heard him speak to the European Community a couple of weeks ago with great eloquence and decisiveness and I know that he will be provocative here as well.

STATEMENT OF ROBERT HORMATS, VICE PRESIDENT, GOLDMAN, SACHS & CO., FORMER DEPUTY U.S. TRADE REPRESENTATIVE, AND FORMER ASSISTANT SECRETARY OF STATE

Mr. HORMATS. Thank you, Mr. Chairman.

First, before I begin my remarks, I just want to follow up your last question about ways of financing adjustment assistance. In the original legislation creating this program, the Congress, in its wisdom, indicated that tariffs should be put aside in a special fund to finance adjustment assistance. That was never implemented by OMB. If you go back to legislative history, you will find that very interesting provision in the law. Now the money comes out of general pool of funds, but your point is extremely well taken. If what the Congress had really intended had been followed up, you would have had more money and perhaps a greater disposition to use it. I will talk about that in a little more detail because I think it is an important subject.

First, let me say again that I think this is an awfully good idea having this hearing because, as your comments initially pointed out, dramatic changes have taken place in the international trading system. Trade, as a percentage of GNP in this country, has doubled over the last 15 years, there have been huge increases in trade worldwide, and a lot of new actors in the trading system, including the developing countries. The United States, which 15 years ago was dominant in most key sectors, now is challenged by new producers, both industrialized and developing, and the quantity of overall trade has just shot up quite dramatically.

Also, the nature of the trading system has changed, as you also pointed out. Today, governments are playing a much greater role in international trade. In fact, for the most part, free trade is more

a myth today than a reality. It is simply not practiced in many sectors of the world economy. As a result of Governments playing a role to support industries where there is overcapacity worldwide, to help industries that are labor intensive, to support their domestic agriculture, virtually every country in the world has imposed some type of barriers. There is a great deal more bilateralism and barter, and it is simply not the system that was originally intended by the GATT. It has evolved well beyond that.

For that reason, the GATT itself has become somewhat antiquated, and rusty, and considerably more legalistic than is appropriate to deal with the problems that we now face.

The question is: What do we do about it? There are several areas that are particularly important.

First, it is extremely important that we regain the momentum for improving the international trading system and I very much support the notion that we need another major new round of negotiations, but not negotiations that are precisely duplicative of the Tokyo round or the Kennedy round—a different type of trade negotiation. I will just make a couple of points about that and we can discuss it later.

First, it seems to me that the past negotiations have been somewhat overly legalistic and that what we need to do instead is to develop, first and foremost, in these negotiations a set of procedures for identifying or prenotification of trade restrictions or trade subsidies. I think this is particularly important, this prenotification point, because then governments can identify the impact of such measures on one another.

Now if we recognize that we are not going to avoid Government intervention, the next best thing is to ask governments to inform in advance the GATT of what they intend to do, the impact on other countries, and also to put in place procedures internally for adjusting, so that those restrictions or subsidies can be phased down and out as soon as possible. In other words, some greater degree of international monitoring, advance notification, and some international obligation to undertake the domestic adjustment measures to phase that government intervention out.

It strikes me that that is not so much a legal problem, although it may involve that, but a problem of developing serious procedures that everyone follows in that area.

Second, in terms of getting negotiations started, we simply cannot wait until all the actors are ready because we will be waiting forever, and much damage will take place in the system while we are trying to pull this together. We ought to think about using what one might call the nonproliferation theory in getting another round started. The nonproliferation theory is, first, to stop the proliferation of new measures, but more importantly, to recognize that if we waited until all the countries that had nuclear weapons were willing to participate in the negotiation of a nonproliferation agreement, a negotiation would never begin.

What you have to do—and I think Bill Brock is aiming at this—is to get the major developed and developing country trading nations involved in negotiation to start developing the new procedures and new rules and then let the others come in later, but not wait until we have everybody onboard. If we wait, we will be wait-

ing indefinitely. I could elaborate on these in a few minutes because I think it is important that we get started and get started soon.

The second main point relates to something Mr. Bergsten said, and that is the link between exchange rates and trade. In the negotiations that took place in fact primarily between the United States and the community, which led to the Tokyo round, the French Finance Minister, Giscard d'Estaing, who was Finance Minister at that point—made a very strong argument that it is hard to negotiate trade when you have monetary distortions and monetary volatility. The American delegate, at that point Secretary Shultz, who was the Secretary of the Treasury said, "No, we should move ahead with the trade negotiation regardless of whether or not the monetary system was in good order."

The French had a point. Exchange rate distortions today are probably the single greatest distortion in the international trading system and therefore, while we should not wait until the monetary system is improved to begin improving the trading system, we ought to recognize the two are very directly linked and we need institutionally, both within our Government and internationally, to develop some forum whereby the financial, monetary, and trade people meet to try to figure out ways in which exchange rate distortions which lead to trade distortions can be avoided. In other words, how do you prevent exchange rates from falling into danger zones which lead to major trade distortions that hurt domestic economies and cause people to ask for protection to offset those distortions? Some sort of procedure and some sort of institutional arrangement—not necessarily a new institution—we can use existing ones—is a good idea.

Third, in the area of the developing countries which Clayton mentioned, there is a tremendous increase in U.S. trade with Third World countries. Most developing countries are not major participants in the institutional arrangements of the trading system, although they are very active participants in international trade. Somehow, whatever we do institutionally in terms of new negotiations, we have to be sure that the major industrialized and developing countries are included in that negotiation.

The last point is on adjustment assistance and I think this is critical. There are two things that I would suggest and I just put them on the table.

We need to have a quicker delivery system. The delivery takes an awfully long time. A lot of people get their adjustment assistance when they have gotten their next job and labor is absolutely right that this is not working very well. And the trade relief system, when it does work, is sort of an all or nothing proposition. For instance, you go to the ITC and the ITC says that you have been injured and imports are a substantial cause of the injury referred to, then you might get some assistance and some protection perhaps. The problem is that sometimes an industry will go to the ITC and imports will not be the major cause of the serious injury so the industry goes away with nothing.

It seems to me that there might and perhaps should be some intermediate zone whereby even if a firm or an industry does not get protection, it can be given, on the basis of an ITC recommendation

associated to some degree with an industry or firm adjustment program, some type of adjustment assistance. In other words, there will be some intermediate zone between protection and no protection, such as measure of adjustment assistance to help the industry so long as that industry has an adjustment plan to improve its competitiveness.

That concludes my comments, Mr. Chairman.

Senator ROTH. Thank you, Mr. Hormats. Just going back to the problem of governmental ownership, which I think is one of the critical problems and a very difficult one to deal with, one of the questions I would hope that we would consider later is how do we deal with this, whether it is a Communist country where everything is government owned or a Western democracy where increasingly, at least in some of them, the governments participate in the market. Can you really govern those trading systems with the same rules as for a market economy or is there perhaps a need for special rules to be negotiated.

Before we get into some of these questions, I would like to turn to Mr. Patterson, who as I indicated brings I think a very key perspective because of his own wealth of experience with the GATT organization itself.

First, I would like to say that we are delighted to have Senator Bill Bradley here. Senator Bradley is a leader in the Senate on trade matters and is a member of the Finance Committee which has jurisdiction over most trade problems.

Welcome to you, Mr. Patterson.

STATEMENT OF GARDNER PATTERSON, FORMER DEPUTY DIRECTOR-GENERAL OF THE GENERAL AGREEMENT ON TARIFFS AND TRADE [GATT]

Mr. PATTERSON. Thank you, Mr. Chairman.

Well, the last speaker on a panel of such well informed and experienced people is hard put to it to say anything fresh, but perhaps I should start off by taking exception with something you said at the very beginning, Mr. Chairman.

If I understood you correctly, you said the principles on which the trading system is now based, that is the GATT principles, are largely irrelevant. I do not agree with that. I think the principles are probably the right ones and they have served us well. They are easily stated; that is, that the world trading system should be multilateral, that there should be most favored nation treatment, only exceptionally should trade barriers be other than tariffs, once foreign goods have crossed the frontier they should be given national treatment. There should be frequent international negotiations aimed at lowering trade barriers. Escape provisions should be spelled out and available and action against "unfair"—particularly dumping and subsidies—should not be permitted and procedures should be set up to settle disputes.

Those principles seem to me to be right and, as I say, I think they have served us very well and they are not irrelevant, in my view.

Nonetheless, the system is clearly not working as well as one would wish, which is perfectly apparent. The defects are both in

the way we are using the system that is, the way members use it or do not use it—and in the areas it does not cover.

As to the former, to make the system perform better, a lot of changes are needed. The ones I would like to mention briefly this morning are, first, that far too many violations of the rules and commitments go unchallenged, and that is very corrosive of the system. This is because often those who should complain do not have clean hands or they do not want to pay the political price of blowing the whistle.

The only answer I see to this problem would be a revolution, and that is that the contracting parties would instruct—not authorize—instruct the GATT Secretariat to put on the monthly agenda of the GATT Council every documented case of a violation and let those who are charged with violations defend them.

This, of course, also leads to the second point I want to make, and that is the dispute settlement machinery. It's far too slow, as Mr. Yeutter mentioned—far too slow and cumbersome, but the basic problem here, again, is one of the way in which panel members are selected, the way in which it is decided who is going to decide these questions.

Now on a more substantive matter, if the system is to be saved, we must vigorously enforce the existing rules on subsidies and come to a much better understanding and agreement than we do have as to what kind of subsidy or subsidy effects are unfair and actionable. This is a very difficult problem, but it is increasingly at the core of many of the GATT difficulties because of the increasing role of all governments in domestic affairs and because of the increased importance of nonmarket economies. But the subsidy problem is critical, it seems to me, to saving the system and it is very difficult to deal with it, as you know.

The next point I would make is that the present tendency, notably in the United States, to deal with trade problems on a bilateral and sectoral basis must be checked or the procedures modified, if the system is to be saved.

These arrangements—auto, steel, textiles, agriculture—they are arrangements that are negotiated between governments and industry in one country and governments and industries in another country, and then between the governments and industries in the two countries, as the case may be.

Now that means that such arrangements are inherently protective because the users are not present in the discussions. They are very difficult to reverse or terminate because a whole bureaucracy of government and industry have been established with a stake in the arrangement. They are contagious because they create difficulties for users, and in a democracy such as the United States, if you help one industry and another industry is in trouble, especially if it is partly because of the higher cost imposed on it because of the first industry, then you have to do something about them.

Furthermore, since each of these arrangements a sort of international trade system of its own, it makes any system of general rules increasingly difficult and irrelevant and, as I say, I think general rules are what we are striving for, not a whole basketful of special arrangements.

If we cannot find ways to stop this practice, at least it seems to me first of all that the negotiations of such sectoral arrangements should be made more public—that is, the process should be opened up so that the users can be heard.

Second, criteria should be established for terminating them.

Third, there must be, I think, some link to industry adjustment.

Let me take another point on a related thing, that is the current flirtation of the United States with these bilateral liberalization agreements—Canada, Israel, the Caribbean Basin, the Pacific rim. I think these bode ill for a well-functioning system as well.

From what an outsider can tell, they fall far short of what could be classified as a customs union. Therefore, since they are going to pick and choose the items that are going to be liberalized with such trade, they are almost doomed to divert rather than create trade. As a consequence, it seems to me the chances are very great that they will create a lot of political tension by those who are being discriminated against, they will move production from efficient to less efficient places, and they will play right into the hands of the Europeans who are far more adept at making deals such as this than the United States is.

I would also agree with everyone who spoke this morning I guess that before the system can be saved, we also have to negotiate some general rules for the graduation of these LDCs. We now have the problem of the NICs in many areas are extremely competitive, and the necessity for their assuming much fuller GATT obligations is important.

The present arrangements where this issue is handled on a bilateral basis are unsatisfactory, creating a lot of unnecessary political difficulties and you get a lot of inequitable ad hoc agreements.

I agree, too, that it is very important that the escape clause be refined and extended. I speak here not just of the selectivity problem which created such an awful difficulty in the Tokyo round, but of the need for stronger rules and clearer rules on the conditions for relief, the type and extent of permitted restrictions, the duration of restrictions, and, again, the necessity of making some adjustment efforts if one is to benefit from imposition of restraints.

Now clearly the role of agriculture in the system is difficult, bothersome, important, and unsatisfactory. I would only say that Mr. Yeutter overspoke a bit when he said there were no rules for agriculture. I am reminded of the importance of the soybean commitment that the United States has in GATT which is of considerable value.

Now beyond these reforms of the existing system, clearly there are areas that need covering. Service is obviously an important one. The trade effects of investment policies is another area that is very important to be brought into the system. More difficult, of course, is this problem Mr. Bergsten touched on and all of you touched on, and that is the importance of coordinating trade policy and monetary policy, but I leave that to my colleagues on the right.

So, Mr. Chairman, I come to the conclusion that the system is worth saving. The principles are relevant. It can be saved, but it will require a lot of work and a lot of difficult negotiations and a lot of changes in U.S. policy.

Thank you.

Senator ROTH. Thank you, Mr. Patterson.

Let me, if I might, just go back to the question of principles. We are sitting around the table because we wanted to have it as informal as possible so feel free if you want to ask a question or interrupt whenever you think it is appropriate.

I was interested, Mr. Patterson, in your comment that you felt the basic principles and premises are as valid today as formerly. Let me just raise two or three questions in this area.

One of the premises of the original GATT was, of course, the free market. It does seem to me that the GATT founders did not anticipate the kind of government involvement, whether it be direct ownership or so-called industrial policy or many other indirect things like nontariff barriers that exists today. So that this seems to me a very significant change from what we earlier anticipated.

Another area is an original GATT commitment to multilateral agreements. The fact is that we have had an explosion or at least a multitude of regional, bilateral agreements. Some of them done within GATT with approval of GATT, others, as you have pointed out, Mr. Patterson, outside the GATT system. If there was one thing I sort of got a general feeling—if I am wrong I would appreciate any member of the panel speaking up—that there is a general agreement that we need some new negotiations. The question might be more as to what the subject matter of those negotiations may be.

Is that the feeling of the panel?

Mr. PATTERSON. My answer to that is certainly yes, but since you made a point on what I had said about the relevance of the original premises of the GATT, I like to say that this increased role of government, not in nonmarket economies but most economies, is far greater than anything that was anticipated when the GATT was created. But the GATT principle there was that subsidies on exports are undesirable and can be actionable. And that is the principle, and that is the right principle.

The question we have now which is so difficult is defining how you make that principle operative. What does constitute a subsidy, because subsidies are not permitted.

Senator ROTH. I think that is the heart of the problem.

Mr. PATTERSON. The heart of the problem is making the principle work.

Senator ROTH. You had the rule, as I understand it, of transparency, and the problem is now when you have government ownership. It is much more difficult to screen out that subsidy.

Mr. HORMATS. There is another point which is that you cannot tell the trade impact of a subsidy. At some point at an early stage, in the research process, a $10 million subsidy could have a billion dollars worth of future trade impact, and one, it is very hard to identify this subsidy because research supports are things we do all the time and they are, to a degree, a subsidy, not envisaged by the GATT and two, a well-timed and well-placed $10 or $15 or $20 million can have a very large trade impact.

The question is, should you counteract it, how do you counteract it and what should you counteract it with? These are very complex issues that the GATT never really envisaged.

Senator ROTH. That is the reason I would be interested in any of your comments about whether we should try to create special rules and special negotiations in this area. For example, I do not think we want to foreclose trade necessarily with a Communist country, but how are you going to determine whether or not it is equitable? What is the thinking of the experts on this?

Mr. BERGSTEN. There is experience on that which Pat could comment on in more detail more than any of us. When you conclude that an economy you are dealing with is not itself based on market principles, then you are forced back to some kind of quantitative rule. When the GATT accession agreements were negotiated with some of the Eastern European countries, quantitative requirements were put in place in terms of the growth of their imports.

The view was taken that tariff cuts and commitments on what we would call nontariff barriers just were not relevant for the reasons you say, but people did not give up. They then tried to apply the principles in a different way by setting quantitative requirements.

That had worked to a mixed extent, but I think it is one way to get over that hurdle. Some people have suggested that ought to be done with Japan. I would not go that far, but there is, again, a tried and true method to work that out I'm sure. Mr. Patterson has the details.

Senator ROTH. Could I just ask you one question and then we will go to you, Mr. Patterson.

Would that have to be on a bilateral basis, or is there any way you could set——

Mr. BERGSTEN. No. That was the purpose of global import levels of the country in question—Poland, Romania, or whoever it may have been, had to commit, as I recall, to a certain level or rate of change of its total imports from the GATT members—as opposed to its trading partners within Eastern Europe. It was trade with the hard currency world.

Mr. PATTERSON. Those requirements were sort of the entrance fee for the non-Market economies. That is, they were the obligation they undertook on the import side. They had to take quantitative import commitments of one kind or another because a lowering of the tariff would have no significance. On the export side—and this problem of whether they are subsidizing exports—that is a problem which some people are currently worrying a lot about and it is clear the assumptions of the GATT are not relevant for determining the existence of subsidies here. Therefore, it would appear that the solution to this problem has to be found in negotiating some sort of arrangement whereby if imports from those countries cause injury—that would be reason, justification for action. But you have to be very careful how you define injury in these cases.

I do not think the problem is insoluble, but it is a very difficult problem and it gets back to this messy problem of how you deal with subsidies.

Senator ROTH. Mr. Yeutter.

Mr. YEUTTER. I was just going to say, Mr. Chairman, that a number of the problems such as that are extremely difficult to handle in the context of the GATT, but as Gardner said, they are not impossible and the problems are not insoluble. You may not be

able to handle them perfectly, as Mr. Bergsten indicated. You have to make do, but making do is better than not confronting them at all and it seems to me there are two points to be made here. One is that there needs to be commitment on the part of the major nations that they confront issues or questions like that in the GATT, and second, that they use the GATT as the mechanism to do it, and not simply strike out on their own on a one-to-one basis. There has been a trend in recent years to ignore the GATT mechanism and simply go off willy-nilly with different ways of confronting these issues. We gradually destroy the GATT when we do that. Perhaps the GATT has to accept some of that responsibility, too, for not demonstrating the aggressiveness and leadership to prevent the erosion of its charter. Nevertheless, there is only so much that the GATT staff can do; if the United States, the European Community, or Japan decides to ignore the GATT and do their own thing, Director-General Dunkel cannot order anybody to come in and say, "Use the GATT mechanism."

The second point gets back to your earlier question about a round of negotiations. Senator Roth, I agree that we do need to get a round underway. A few years ago I would not have said that. While I was immersed in the Tokyo Round, I concluded that it would probably be the last major round of negotiations and that we would do it differently from then on for a variety of reasons. I have now changed my mind. I am not so sure that it is desirable to have a gigantic round of negotiations, in that it is very costly and requires an enormous commitment of manpower. But I am convinced that such a commitment is necessary to save the system. That is really the point you raise here; we need it because if we have a major round of negotiations it will force the principal trading nations of the world to be committed to the success of the round and that alone is helpful.

Senator ROTH. It starts that bicycle motion?

Mr. YEUTTER. It gets the bicycle moving and commitment is the name of the game. If there is not sufficient commitment on the part of the major trading nations, the GATT will not succeed, and maybe not even survive. One way to force the hand of all the major participants is to have serious discussion and intense debate on this very point. And I think for that reason we should do it.

The other point I would like to make is that this is all an educational process. There are still only a handful of people in this world who understand what international trade is all about and what the benefits are. For that matter, there are only a handful of people in the United States who understand it.

I picked up USA Today yesterday and read a feature article about a lady from Alabama who is giving speeches calling for an across-the-board increase in tariffs on all imports coming into the United States. She is convinced that there are essentially no jobs involved with exports, and lots of jobs involved with imports. Therefore, the way to improve the U.S. economy is to stop imports. She says that she has given hundreds of speeches and she has yet to find anybody in the business world who disagrees with her.

Well, it just seems to me that if that is the case, we have a long educational process in the United States, let alone internationally.

But my basic point is that having a round of negotiations adds a positive element to the educational process. The press and the media focus on it. People learn more about trade and learn the benefits of trade.

Senator ROTH. Senator Mattingly.

Senator MATTINGLY. I would like to comment on the educational process to which you refer. In this regard, the trade system may be shot. I think trade policy is very similar to tax policy. It is too complicated. You talk about loopholes in the tax policy, well, trade policy is full of loopholes, and it really does not meet the needs of today's world.

The current policy of the GATT is falling by its own weight. That is what I see happening. You talk about this lady going out and talking. At least she is talking. We talk and Mr. Dunkel talks and Mr. Dunkel says we are at a crossroads in our trade relations. We've probably been at the crossroads for quite a while. I saw last year or the year before last when the GATT was held—the first one they had held in 9 years I may add—that the GATT is not pressing the issues that ought to be raised.

I guess my question would be to the four of you—how and when do we go about either modernizing the GATT? We know about evolutionary world economic changes and we saw what happened during the last GATT conference. Traditionally, the GATT has not met with the IMF or any other financial body. The Congress even approved in the IMF legislation an amendment I offered in which we said, "Please try and meet with them." Yet they have not. Now they are really not doing their job. And the thing about it, if we are going to reform this, who is going to reform it? The U.S. Congress is not going to reform the GATT.

What I want to know is how and when—when should be now—but what are some ideas? Do we try to get, as has been suggested, a super GATT or get participants together in any room like this—when do you do that and how do you do that? You all have been in this longer than I have. How can you go about doing something like that?

Mr. HORMATS. I would like to make a couple comments on this because I think this is a critical question—how do you do it and when do you start?

One of the problems with the GATT is that it tends to ask the wrong questions. The GATT debate tends to be over what is legal and what is not legal—legal in GATT terms.

Senator MATTINGLY. Let me interject before you go on. The reason why multilateralism is not working is because of the GATT. That is the reason why trade has become more bilateral.

Mr. HORMATS. I think that is part of it. The GATT is really a mirror. It reflects the intentions and the desires of its participants. If the participants wanted it to work better and wanted the Director-General to have more authority, they could vest that authority in Mr. Dunkel—who is an excellent man—and thus could make the system work better.

The problem is that it has gotten bogged down in legalities. The community says its agricultural practices are legal. We say they are not legal. And a lot of other issues are not even taken up by

the GATT because people says the GATT rules do not address them.

It seems to me that we have to start by asking a different set of questions, not whether something is legal or illegal under the GATT, but whether it is distortive of trade or is not distortive of trade and whether it promotes adjustment or does not promote adjustment. These are the more fundamental issues that we have to deal with. The question is, how do you get there?

This involves a major change in the approach. Instead of sitting down and trying to rewrite in excruciating detail the bylaws of the GATT, which will take forever, we have to figure out procedures for identifying whether and to what degree actions by countries are distortive and whether and to what degree they promote or retard the adjustment process.

If we do that, we can force people to notify the GATT in advance of what they are going to do and to indicate and alleviate the impact of other countries, and what they are doing internally to promote the adjustment process so that those measures they impose can be phased down and phased out. Those are the three key elements.

The other point on the Director-General question is that we should give the Director-General more authority just as we have been willing to do with the Managing Director of the IMF. The Managing Director of the IMF has the last 3 years played a much bolder role in the monetary system than any of his predecessors, and he did this in part because he is willing to take action, and in part because everybody realized the situation was so critical that we had to vest one person with a greater degree of authority, we had to give him the authority to tell countries and tell banks to pull their act together and help to deal with this debt situation.

It seems to me you could do very much the same thing with the Director-General. Give him a mandate, even if it is sometimes painful from our point of view, as it will be. But if we are interested in promoting our trade interest, he has to be able to play a stronger role and exercise a greater degree of pressure on countries and we—all of us have to be willing to go along with that.

Senator MATTINGLY. How do you give him a stronger role?

Mr. HORMATS. If you were to take Mr. Patterson's thought and have him go in and ask governments to notify and give advance warning of what they are going to do, assess the impact and things of that sort, it could be done without any changes in the bylaws. He has a lot of personal authority to do this without changing the bylaws, just as the IMF Managing Director did.

Senator MATTINGLY. Who calls him on the telephone and says, "Arthur, we want you to begin work?"

Mr. HORMATS. If the several major countries in the trading system did that he could do it. I am not saying this is the kind of sequence; I am just saying it could be done.

Senator MATTINGLY. In other words, what leverage does he have? The IMF has got the dollar leverage. What leverage does Mr. Dunkel have other than living in a nice place?

Mr. HORMATS. He has less leverage than the Managing Director of the IMF. But he has more credibility, if you want, or could exert more authority than any other single person in the trading system.

Senator MATTINGLY. How do we impress on Mr. Dunkel or whoever it may be, the importance of exerting more influence?

Mr. YEUTTER. That depends to a considerable degree on the personality of the Director-General, how aggressive he is prepared to be, and how often he is prepared to put his job on the line to stir things up. Typically, we have not had Director Generals in GATT who have played that kind of role. It was done a good many years back, but over the last 10 or 20 years there has not been much of that.

In my judgment, that has to change and, Bob is right. The Director-General can do that on his own if he is willing to take the personal risk. I wish he were and I hope that he is.

But beyond that, it would certainly help if four or five major trading nations said, "Arthur, we need to get a handle on this trade problem and the only person in a position right now to knock some heads together is you. So, start knocking them together."

It seems to me that leads to a second point. Senator Mattingly, which is that the GATT has to be flexible and Mr. Hormats was really alluding to that. We still think about going through tariff negotiations and we think about getting 88 countries together in a room talking about things. It seems to me that we ought to determine what the priority trade problems of the world are and then Mr. Dunkel should say, "How do we get on top of each of these?" If getting on top of a particular issue means bringing 10 people into the room and sitting down to work on it, then the GATT ought to get those 10 to Geneva or wherever they are going to work on it. If it requires 20 people, let us get 20. If you have to go to Washington, Tokyo, or Paris, let us go there. If you have to have both the Trade and Finance Ministers, then let us call them both in.

There has to be some creativity and imagination on the part of the GATT to confront these major issues.

Senator MATTINGLY. Now how do we get those members to do that? I have been to a GATT ministerial meeting once and if it is going to be every 9 years——

Senator ROTH. Let me throw out one possible thought on this. I think you are alluding to it in what you are saying. Would it be helpful if there was some standing authority for continuing negotiation of some sort? Would that give him any clout or any assistance?

Mr. HORMATS. I think so. The CG–18 is sort of a steering group of the GATT. It was supposed to play the role of an ongoing advisor to the Director-General and to create some momentum. If you had a permanent type of negotiation you would help enormously. That is where you could get the sort of notification, monitoring, phase-out monitoring policies—and that would strengthen his hand also.

Mr. PATTERSON. Just two or three points on this, Mr. Chairman. First, on the role of the Director-General, the head of an international organization cannot do anything unless he has got two or three critical countries supporting him. If the United States and the Community or the United States, the Community, and Japan preferably, want something done, it is done. But if any one of those says, "We will not have this," there is nothing you can do.

For example, my suggestion that the Director-General should be instructed to put documented violations of the GATT on the record,

if the United States were to say, "Look, we will not attend a meeting where that is done; we will not have it," it becomes ineffective. But two or three governments can do it, and if they want to do it you can do almost anything.

Mr. YEUTTER. Mr. Patterson, that is a copout because one can use that as a rationale never to do anything. All you have to do is say, "Well, gee, we cannot get the EEC to agree to this or we cannot get the Japanese to agree to that." I think you have to say, "It's the job of the Director-General to get those people together and figure out a way to do it."

Mr. PATTERSON. Yes, but that is the easy answer. The question is, unless in the end you can get them to agree—you do not have to get everybody to agree; that is my point, but you do have to get two or three to agree and you do that by an awful lot of private discussions in the back room, but for the Director-General of any international group to march out without working it out behind the scenes is ineffective.

Mr. HORMATS. Nobody suggested that. Of course, you have to get a critical mass of support for him.

Mr. PATTERSON. Sure. And a critical mass is not very many.

Senator ROTH. And you also need some strong leadership.

Mr. HORMATS. Yes. He has to be firm.

Mr. BERGSTEN. I would comment on one aspect of the analogy that you both made to the monetary side and the trade side. The analogy does not quite hold, unfortunately, not only because the IMF has money to use and the GATT does not, but because the nature of the problem is different.

In the monetary system, whether it was exchange rate crises under fixed exchange rates in the 1960's or threat of default by major debtor countries today, you are looking over a brink. You are facing a real crisis, which could have massive real world effects if not corrected.

The governments frequently find difficulties working that out themselves, but they would at least acquiesce in an initiative taken by the Managing Director of the IMF or at different points the Chairman of the Federal Reserve Board to deal with that problem in a decisive way.

Trade problems are not of that nature. They are not system-destroying problems, except once in our history—and even that was not seen at the time as having the kind of devastating impact that it did over a period of years.

What we have on the trade side is a more erosive process where barriers and subsidies and such pile up and erode the system. Over time, an historian can look back and say that we faced a watershed and did not cope with it. But it is not the same crisis environment that you get on the monetary side.

Therefore. governments have been unwilling to delegate to anybody the authority to take initiatory steps even of the modest type Mr. Patterson suggested. Mr. Patterson's proposal is very important and should not be lost sight of. Why should not the GATT Secretary have an obligation to come in once a month or once a quarter and say that the following violations have occurred, and what are you going to do about it? That seems simple, but no government has ever taken the initiative to propose that the GATT do

that. They have tried to do it in small groups but one government or another has said, "We would not want that to occur because it violates our sovereignty." What people do not realize is that nominal sovereignty is far greater than real sovereignty and that they have to accept some changes of that type.

However, the fact that it is an erosive process, not a crisis that is going to erupt on you the next day if you do not cope with it, is a critical difference, but I think the same approach nevertheless has to occur. The big players, two or three, have to be willing to see it the same way and either take action themselves to change the rules or just move on the negotiation or give initiatory authority to the international civil servant to do it.

That has basically happened on the monetary side. I used to represent the United States on what is called the Group of Five Deputties. They get together, sometimes every week or so, depending on how critical the issue is, and basically are the steering group for the system as a whole. Everything is ratified and eventually implemented through the IMF, the global body, but you have to have the steering group. The CG–18 team is too big. It does not do that.

There have been set up over the last few years so-called quadrilaterals where the United States, the Community, Canada, and Japan have met to try to play that role. So the instrumentality is there, but they cannot see that the risk of continued and escalating erosion is sufficient to get them to take action.

Now, as I said before, some of that goes to the monetary side and some things outside of trade per se that make it very difficult even for the trade people who want to move to be able to do so, so I do not think the trade people by themselves can quite do it. But that is the structure and it is a very different basis here which makes it more difficult.

Senator BRADLEY. I think the theory of the benign dictator is one that, as you point out, has some major flaws in it. I have two questions. You recommended that every month the Director-General post those trade-distorting practices that have occurred in that month. Where do we now have on record available for everyone all the trade-distorting practices that have occurred in the last 20 years and how do we begin to highlight what already exists before we decide the highlight what is added?

Mr. YEUTTER. If I may, Mr. Chairman, I would like to embellish that a bit because people have begun, Senator Bradley, to think about it in a couple of different ways. There are obviously a lot of trade-distorting practices around, including plenty of them that the United States itself has created. One of the problems in dealing with those, Senator Bradley, is that most of the world does not recognize that they are distortive because nobody points out the trade-off in costs and benefits.

This issue was raised by Bill Carmichael of Australia sometime ago and he did a paper on it. The thrust of that paper was that we ought to make an effort to get all countries in the world to be more transparent in their trade actions because typically the consumer pays a price for protectionism but the consumer does not know it, and it is well hidden in the governmental process. We could use voluntary restraint agreements on automobiles as a classic exam-

ple of that. How much did those agreements cost the U.S. consumer of automobiles. But there are a lot of others.

We have a committee now that is chaired by Olivier Long, a former Director-General of the GATT, with representatives from people around the world working on the question of how one can make these kinds of trade decisions within given countries a lot more transparent so the general public recognizes what the cost-benefit and tradeoffs are.

Senator BRADLEY. So you are saying that there is no place that anyone can go to find what the distortive trade practices are that the GATT is supposed to prevent. So the only way we know if someone is violating GATT is if they voluntarily say that they are violating GATT or if the complaining parties state that, "We think country X is violating GATT." Is that right?

Mr. YEUTTER. That is essentially right.

Mr. PATTERSON. That is pretty much correct. And I think the problem is, you have to start someplace and it is probably not possible to get all the past violations. But my guess would be that if you read carefully the Financial Times and the New York Times and Le Monde, that you would pickup a very great many. And once the process started, you would find other people coming on and saying, "Did you know what the Community did last week?"

Senator BRADLEY. So we turn GATT into the IRS?

Mr. PATTERSON. Well, you turn it into an enforcement agency.

Mr. BERGSTEN. The SEC.

Senator MATTINGLY. But what you need is to reform GATT because right now it is ineffective. That is the bottom line.

Senator BRADLEY. I have one other question if I could. Mr. Hormats talked about and many people talked about how trade and monetary policy are related and how you need to have some place that you can begin to discuss the tradeoffs in a systematic way.

Other than that suggestion, I have never really heard a specific proposal as to how that could be done. What kind of institutional arrangement would allow that to occur?

Mr. BERGSTEN. The problem in answering that is there are different institutional arrangments within different countries. For example, ask yourself where that coordination is done within the U.S. Government. To the extent it does, it is probably a different place than it is in the French Government. I can tell you that for sure. It changes from administration to administration and within administrations. That is the underlying problem.

At the international level, there are plenty of places. The OECD is in some sense the natural place to do it, where you do have frequent ministerial level meetings, and you have a Working Party of Three that focuses on the monetary side within the broader context of the Economic Policy Committee. You have plenty of meetings and groups, but again, to come back to the gut politics, you need to identify within each government the closest thing your have to a Czar over international economic policy. In some cases, it may be the Secretary of the Treasury. In some cases, it may be the USTR. Under Senator Roth's bill, it would be the Secretary of his new department. It may be two people. And there has been the recent idea to set up meetings of Finance and Trade Ministers coming to-

gether from each of the major countries to try to pull it together in the way you suggest.

It would probably have to be a somewhat flexible cast of characters, but the principle is the right one. It could be started on an informal basis, like the Group of Five Deputies that I mentioned that became central to the monetary system. There is no constitution for that. It is not written up anywhere. It is not endorsed by any international legal agreement, but it has existed now for about 20 years of practice and it more or less has done a good job in coordinating international monetary affairs. Now it could be broadened by either having the person who is the Czar, or it could be a triumvirate I suppose within a given country, come to that same table. You have to keep the number of countries down, of course. We are only talking about five or six at the most, so it is a manageable group, and it would have to be done in the first instance informally.

Mr. YEUTTER. Those kinds of meetings, Senator Bradley, could certainly be done under the aegis of the GATT. In other words, it is not all that difficult for the Director-General to determine and identify who the key players are in each of six or eight countries and bring them together. That is what leadership is all about and that is the key to doing it.

Senator ROTH. Could I intrude here, because we're not going to finalize, I am sure, any of these areas, but time is moving on and there are a few other areas I would like to have some general discussion on.

It seems to me that there is some consensus here that there is obviously a need for institutional reform. Part of that reform depends on strong leadership. Part of it depends on some kind of a continuing authority to negotiate so that there is some power, that there needs to be at the international level some basis of consulting and discussing monetary-trade relations. Earlier, somebody made some kind of suggestion that it is important that when there are problems there be some kind of a timeframe, which Mr. Patterson points out is difficult because of some of the questions of how you appoint those who participate.

These are issues that we would like to explore further at some future time, but I would sort of like to turn back for a moment to the question that we talked about having negotiations. There seemed to be general consensus that there ought to be some kind of a negotiation.

We really have not gotten into any detail as to what should be the timeframe of that; what are the issues that should be paramount. So I think it might be interesting—I think you have to leave, Mr. Hormats, to catch a plane——

Mr. HORMATS. I am all right.

Senator ROTH. Maybe we have a little more time than we anticipated then.

But let me just go back for a moment. What kind of a timeframe are you talking about? Are there any specific thoughts on that?

Mr. PATTERSON. May I say that apart from a general decision to have a big wide-ranging negotiation, it seems to me the facilities on these various codes that were negotiated—each code has a committee, such as the subsidies committee—the code committees can be

used any time countries want to negotiate. It would seem to me that rather than getting involved in the endless hassle of trying to get an international agreement about a wide-ranging negotiation, just get those who are interested in the problem of government procurement where there are some huge problems still remaining, or the subsidies, which is the biggest problem of all, to use the code committees. This is not working well, and you could simply sit down and try to improve it. You can do it within the code framework.

Senator ROTH. Could I ask you a question there? How would you negotiate agricultural questions? Could you negotiate the question of government ownership through these codes?

Mr. PATTERSON. If one chose to tackle the problem of trying to negotiate better arrangements for dealing with subsidies, I think you can do it within the framework of the committee that was established when the subsidy code was signed 3 or 4 years ago. Now what you then choose to negotiate about is a matter that you get other people to agree to negotiate.

Senator MATTINGLY. What negotiating parties are you talking about?

Mr. PATTERSON. I am talking about the Community, the United States, Japan, and Brazil.

Senator MATTINGLY. Who are the negotiators, though?

Mr. PATTERSON. Well, I do not know who the United States is going to appoint. You see, nobody can choose who speaks for the United States except the United States, but they would have to appoint someone to negotiate and you would have to get the major parties to agree that the time has come to recognize that this business on subsidies is not working well. We have got to tackle this problem, not only with respect to non-market economies, but also the problems arising from increased state ownership in market economies.

I do not think you need any decisions by Ministers as such, but you have to get the others who are critical in the business to agree. You have to get the Community to agree.

Mr. BERGSTEN. I disagree with Mr. Patterson on that at the strategic level. He is certainly right that we have code committees and they should be doing more than they are, but I disagree with him for two reasons.

First, I think it will not happen simply in its own narrow confines. The history of trade policy shows that one has to put the specific issue in a broader context which can seize the attention of political leaders, mobilize domestic support, obviously through the Congress in our country, for a major initiative moving in a liberalizing direction or rulemaking direction.

The second reason is that the whole is greater than the sum of the parts. I place great emphasis on the bicycle theory, the momentum notion, and I think you actually want to take individual components like a new negotiation on subsidies and put them in a package to help you get that whole new thrust in the expanding and equitable direction that you are advocating.

If I had a choice between 10 code committees each going off in its cubbyhole and working versus the 10 doing that plus a few other things in the context of a broad round and the outcome was the

same, I would take the second because of the net impact. Furthermore, I would argue that it is more likely to occur.

The trade policy is a paradox. It is easier to pull off big deals than little deals. Little deals are very hard to pull off because each one runs into a panoply of particularistic, rather parochial narrow interests which can usually block progress or indeed reverse things when handled on its own in a cubbyhole. It is only once a decade that you pull this off, but I think it is true that a bigger deal is more feasible than a little deal. And that is important here in the Congress. The analogy with tax policy is probably right in terms of a big tax reform package versus a specific statute on a tax revision. It is something that you want to keep in mind, at the strategic level, to answer your question as to how to save the system.

Senator ROTH. The reason I strongly agree with you is that as far as this country is concerned, Congress guards very zealously its prorogatives under our Constitution on its rights in trade. It seems to me if you do anything really very meaningful. it would have to be clear that it had the active support of the Congress.

Mr. BERGSTEN. Absolutely.

Mr. HORMATS. On timing. I think this goes along with a point you just made, Mr. Chairman, that if we are going to do it, we are going to have to work very hard between now and the beginning part of next year because I do not anticipate we are going to be able to start it this year before November at least, and, in particular, we ought to take advantage of the London economic summit because that is the time that the leaders are going to get together, and if they can do two things in the typical summit communique language: First, stress the need for regaining the multilateral momentum for improving the trading system; and second, identifying, in credible terms rather than rhetorical terms, three or four of the key objectives; they can at least set their people going to put together the negotiating process.

I am afraid if we wait a whole year until the next summit, we will have a lot of damage done to the system. So in terms of timing, I strongly urge that Members of the Congress who are concerned with this get the administration to focus on that as a priority for London.

Second, on the political point, we have seen in the past that you need a critical mass of political support domestically to be credible internationally. Where we have been strongest is when the negotiator has been seen visibly to have the support of the Congress and the President. The case of Bob Strauss is a good example. For that reason you have to put together a large enough package to make sure that that support is generated at the highest possible level.

In the way you conduct a negotiation, Gardner may be right, that you may be able to find some way of limiting the numbers involved in the various components of the negotiation, but it seems to me you have to have at least some broad, politically supportive grand design, and then you implement it in whatever way is practical. But simply to do it in small closets is not going to work. You need a critical mass of support. I really at this point, unfortunately, do not see that there is a consensus in this country to generate that support. That is what disturbs me more than anything.

Senator MATTINGLY. I agree with you. Of course, Senator Roth would agree, too. I think we all agree that discussions of trade policy were to be placed at the same level of importance as discussions on monetary policy and fiscal policy. This means that trade has a way to go, but we are in dire straits because trade has not reached there yet. That is what concerns me when we start talking about the staff people or whoever it is going over there and negotiating a round. We need results now. But, I think you are exactly right. I think this London meeting needs to be sort of a kickoff for that. It is a heck of a lot easier to start at the top and go down than it is to start down here and go back up.

I was a little bit disappointed last year when Ambassador Brock was not even invited to attend the Williamsburg summit.

Mr. HORMATS. Can I just follow up on that because one thing that was done when Bob Strauss was there was to make sure that he went to those summits. He not only went. The fact that he was asked by the President of the United States to go into the room, sit down at the table, and make a presentation was an extremely important substantive and symbolic act both, because he was there and that made other countries bring their trade negotiators there, and you got a political sense of engagement. And correctly, from the point of view of history, history has made the judgment that those summits were instrumental in moving the process along and I would strongly recommend that the President be encouraged to bring the USTR in. As it stands now at the summit, the Secretary of State and the Secretary of the Treasury sit there throughout the negotiations. I think for the trade part of the negotiation—this is more than a procedural point—that the USTR must be invited to come in and make points and sit next to the President to move this along.

Senator MATTINGLY. I agree.

Mr. YEUTTER. Two quick points just to supplement that: I agree with what both Mr. Hormats and Mr. Bergsten had to say. The London summit is a key element of this and I know there has been a lot of preliminary discussion already. If they can lay the groundwork at the London summit, there is no reason why this process could not get underway as early as late 1985, and, in my judgment, the sooner, the better.

There are some areas for which, in my opinion, we can generate strong public support in the United States, one of them being an area we have not even talked about yet this morning, and that is services. Bill Brock is right in asserting the importance of that area, which is absent from the GATT at the moment.

We in the United States have a lot at stake in the services area and that clearly ought to be one of our priority agenda items.

Senator ROTH. Is it not also true with respect to agriculture and high technology?

Mr. YEUTTER. Yes, especially agriculture. High technology is a difficult area for me to evaluate because I am not sure what high technology means in the GATT context. One of the problems of dealing with it in the last ministerial meeting was that the U.S. delegation could not persuasively articulate what high technology meant. Aside from that, on the agricultural front, yes, and it cannot be done only in the individual committees. They certainly

have a role to play, as Gardner suggests, but agriculture needs to be looked at in its overall context. We simply cannot afford to spend $20 billion a year on agricultural support programs in the United States, have the European Community spend another $20 billion or more, considering participation of the individual EC countries, and have comparable expenditures elsewhere in the world. The whole agricultural structure just does not make sense today and it needs to be dealt with.

Senator MATTINGLY. Just to add on that, looking at the case example. You see it all over the world—with Kohl, dealing with trade directly in that country, with Mitterrand dealing with trade directly, and Nakasone dealing directly with trade, for their respective countries. But when you come to the United States you have "who knows" dealing with world trade. Instead of the President dealing directly with trade issues, you have to send somebody—I cannot even remember his last name—to deal on that issue, and you wonder why you do not win when you go to trade negotiations.

Mr. PATTERSON. In my view as an outsider, the United States often is a very good negotiator. The United States has struck some very good deals in negotiations.

Senator MATTINGLY. They used to; you are right.

Mr. PATTERSON. But the point I wanted to make was to make it quite clear on the issue of when you are negotiating and how you do it, clearly a wide-ranging negotiation is vastly preferable. There is no question about that. For all the political reasons and the tradeoffs.

My point was that if you cannot do that, if that is not possible, then you do not just have to sit on your hands. There are other mechanisms and procedures that should be used and the important thing is to be doing something, not nothing, it seems to me, in the situation at the moment.

Senator ROTH. That brings me to a point I would like to raise and that is a question of, do we want to rule out all types of bilateral or regional approaches? As I said, there have been a number of them that have been done outside the GATT; there have been some that have been done within GATT. Some people, as I understand, argue that bilaterals are fine as long as they're public and everybody can agree or join them if they agree to its terms and so forth.

Is this another vehicle we should look at as a means of expanding trade?

Mr. BERGSTEN. I would not rule them out. Indeed, in some cases, I would advocate them. At the moment, I think they are probably a useful way to proceed. As I understand and interpret what has happened in the last couple of years, Bill Brock and the administration set out initially to launch a multilateral negotiation of the type we are talking about. They made a run at the GATT Ministerial in November 1982 and flopped, I think in large part because they did not have top-level support here. There was a lack of internal consensus that went a long way to explaining that flop. Nevertheless, the multilateral effort did not proceed.

That having occurred, and given this bicycle theory and the need to be moving forward whenever one can, the fallback was to this series of bilateral and even sectoral approaches to try to at least

provide some forward liberalizing movement in a world where the multilateral approach, at least for the moment, had proved infeasible.

Now given that strategic setting as I would interpret it, I think the effort to move forward in the bilateral and sectoral way is less bad than doing nothing at all. You have to do what you can. It is second best, but I do not think it is necessarily inconsistent with moving on the multilateral front.

However, there is a very dangerous incentive in the setup. If you become enamored with bilateral and sectoral deals so much that you forgot the multilateral approach, then you can head off in the wrong direction. I would sometimes in fact criticize the Europeans for having done that—the Common Market itself, preferential arrangements, the European monetary system, etc.

On the other hand, if those things are viewed as way stations toward eventual multilateral movement or viewed as adjuncts to multilateral movement, then I think they are OK. It is not a per se judgment for or against, in my view. It is how they fit into the broader framework, what the alternatives are at a given moment, and how they are carried out.

Senator ROTH. I think I see your colleague disagreeing.

Mr. PATTERSON. I think they are an extremely dangerous way to approach this problem. If you take the cases that we read about in the press—Canada, Israel—these seem to me to take time and energy that might far better be spent on planning and preparing for a multilateral approach, and I think that if they come off they are likely to be a very dangerous, limited and disruptive influence.

Think about what would be in a bilateral agreement between Canada and the United States. Once you start saying it's not to cover all products in which we trade—as a true customs union requires—but we are going to pick only some commodities in which we trade, you are in trouble. Obviously, the United States does not want to pick imports from Canada that will throw American business into trouble. What they really want to do in a case like that, if you can pick and choose, is pick items from Canada that you are already buying someplace else and, therefore, all you are doing is changing the location but you are not damaging the producers of that item in the United States. The Canadians will want to do the same thing. We might be willing to buy more paper products. We have been buying them out of Sweden and if we have a free trade area with Canada we would buy from Canada and have the same amount and do Canada a favor, but it creates an awful problem for Sweden.

That is the tendency, once you can pick and choose what it is you want to import, and once you have done that, then you have created a lot of irritation and you have created a condition in the country which makes it difficult to have multilateral negotiations later because somebody now has a stake in the preferential arrangement.

It is interesting to recall that one of the great problems we had in the Tokyo Round in getting a reduction of imports into the European Community from developing countries was not that the Community was not prepared to do it, but the African states, who had preferential arrangements, would die before they would con-

sent to the Community lowering their barriers on these goods to South America. It is perfectly understandable. The result was very little happened.

I think that is the risk of these small arrangements, as long as there is any hope at all of putting your efforts, and energy, and talent into doing something on a multilateral basis.

Mr. BERGSTEN. Mr. Patterson, we have an example. You can test your thesis in the United States-Canadian context, the auto agreement. Do you regard that as a good or bad thing in retrospect? Do you regard that as trade creation or trade diversion?

Mr. PATTERSON. Well, I do not know enough about the details of that. The automobile agreements are so complicated.

Mr. HORMATS. That is a little bit unique. That is one industry and one labor union.

Mr. BERGSTEN. But was the bottom line the disruptive outcome that Mr. Patterson suggests would inherently flow from these things, or was it more constructive compared to the realistic alternative which at the time was Canada going to a very restrictive auto policy?

Mr. HORMATS. Well, it was surely better than that.

Mr. BERGSTEN. That is the issue in the real world.

Mr. HORMATS. It is a question of whether you do that or whether—it is a question of extent. There are various examples. I would argue that the multilateral fiber agreement was better than not having it at all because if you did not have it at all everybody would have protected their textile industry, but the real question is how many do you want. It is really a question of limits. There are certainly examples, you are right, that are better than the alternative.

Mr. YEUTTER. I empathize with Mr. Bergsten's position. It seems to me that you cannot generalize on bilateral agreements as to whether they are good or ill. You have to look at the specific agreements and you also have to look at the followup. If that bilateral agreement, even though it may distort the multilateral context in a transitory way, will lead to additional multilateral benefits, then it is worth doing. If it is going to distort multilaterally, as Fred suggested, then it should not be done.

So one cannot make, per se, value judgments on bilateral arrangements.

Senator ROTH. It seems to me, if I could get the consensus on this area, that everybody would basically prefer to do it through the multilateral basis but that there are certain—with the possible exception of you, Mr. Patterson—that there are circumstances where other agreements, particularly where they would help promote trade rather than otherwise, that they can be desirable. Is this something that conceivably could become part of the GATT negotiations; in other words, try to lay down to some more definite terms and conditions where regional or bilateral agreements might be negotiated?

Mr. BERGSTEN. There are some rules now, as Mr. Patterson implied. One could apply to that area the same kinds of new proscriptions he was mentioning in another context—transparency. One could do that.

I was just going to say, though, that there is one area where I think we may badly need a bilateral agreement now. It has not been mentioned, though you mentioned the country early on, and that is Mexico. I think most of us would clearly prefer that Mexico join the GATT. I worked long and hard on that when I was in Government. It was a very close decision, we're told. The President of Mexico decided against it and it is probably not going to happen any time soon.

In the absence however, of any arrangement, multilateral or bilateral, United States-Mexican trading relations are evolving in a most unfortunate way, with proliferation of countervailing duty cases and the like, given the absence of any basis now for dealing with those problems. It is our third biggest trading partner and its debt crisis is, of course, of enormous importance. In that case, given the political unlikelihood of getting Mexico into the GATT or even into the subsidy code any time soon, we probably need a bilateral deal.

And that maybe heightens the point that in some cases it is, at least pragmatically speaking, the preferable way to proceed.

Senator MATTINGLY. There is no incentive for them to get in GATT. Why would they want to join GATT? You made a comment, which I want to come back to, about the GATT being a flop in 1982—I think the U.S. flopped. But I think the 1982 GATT meeting exposed the fallacy of GATT. It brought to public view more so than ever our trading partners use of subsidies, whether you want to call them legal or illegal. It provided a high visibility. We were talking before about trying to educate people. I think the 1982 GATT meeting marked the start of the education process in the Congress. There are a limited number of people—Senator Roth and maybe a couple others over in the House—that really understand the trade issue. Yes, I believe more are beginning to understand it now. But, getting back to the GATT and why would Mexico want to join—which they will not—I think bilateralism is going to increase, not decrease.

One other thing we have not addressed is increasing the use of countertrade on account of the debt problems.

Mr. BERGSTEN. I would agree with Mr. Patterson, though, on his basic defense of GATT principles with all the shortcomings and experiences you point to. We would have to invent it, or something like it. Of course, it could be different from what it is now, but we would have to have something like that.

I think Mexico has enormous reasons for wanting to join the GATT, simply to be at the table where a lot of key decisions are made, to get the protection of tariff bindings against it, and, most importantly for the very pragmatic problem it faces right now, having some access to our injury test when subsidy issues arise. They would have to join the subsidy code as well as GATT to get that, but that would be an enormous difference. Look at the difference between Mexico and Brazil today. I negotiated a subsidy code to deal with Brazil where the Brazilians agreed to phase out all export subsidies over 4 years in return for getting the injury test in the United States in joining the subsidy code.

So today when the U.S. steel industry brings cases against Mexican and Brazilian steel exports, there's an enormous difference.

Brazil not only has to be shown to be subsidizing but those subsidies have to be shown to be injuring American industry. In the Mexican case, they do not.

Senator MATTINGLY. Brazil, despite the GATT, has not reduced their subsidies. I can assure you of that.

Mr. BERGSTEN. I can assure you they have.

Senator MATTINGLY. I am aware of many industries, like if you take the aircraft industry and the poultry industry, that would be happy to come up here and tell you all about it.

Mr. BERGSTEN. They still have some subsidies.

Senator MATTINGLY. They would do that today?

Mr. BERGSTEN. They still have subsidies, but as of 1978 they had an export subsidy averaging 35 or 40 percent on all their products. They agreed to phase all those out over a 4-year period as part of the deal. Now I did not want to mention this, but the current administration let them off the hook a little over 1 year ago, partly because of the debt crisis. The administration let them cease to phase out on the schedule that had been solemnly negotiated 4 years ago, and keep the injury test.

But the deal—you asked why would a country want to join the GATT—gives Brazil access to the injury test. Mexico does not have it. That is a big difference and incentive for Mexico to participate.

Mr. HORMATS. I would like to mention the bilateralism in a different context, which is the barter question. This is another vastly new dimension to the system and I think going back to principles, there are examples of pragmatic bilateralism and much as economists regard barter as something somewhat impure, it creates real economic activity that would not be there if there weren't barter or countertrading arrangements.

I, for one, think that if the alternative is not to have a bilateral barter deal, which means less production in the two potential parties to the barter deal, if there is a choice between that and having it, I much prefer to have a barter arrangement or countertrading arrangement.

The question, of course, comes down to whether you can have some general guidelines to ensure that these do not proliferate to the point that they distort the trading system. This really is another thing that is going on completely around the GATT. It is a totally non-GATT issue. GATT does not talk about it to any degree that I am aware of, but Fred's right, that is a good, pragmatic way of creating trade that is not created before.

Now how do we blend that into a multilateral system? I do not have a clue at this point and it may not be important. It's like the Italian economy. One does not need to record the numbers to know that it works pretty well. It is not so inefficient as one might think. But the GATT ought at least to be aware of these practices and try to develop some broad guidelines to avoid distortions—recognizing that frequently barter is better than nothing. It is not perfect, but it is better than nothing.

Mr. YEUTTER. Three points. One, back to Senator Mattingly's comments about the LDC's and the incentive for a country like Mexico to come into GATT. Obviously, when we talk about GATT membership for the LDC's, that is a combination carrot and stick

issue. There certainly are carrot reasons for them to join the GATT and I think Mr. Bergsten articulated those.

What we have not begun though is to apply much of the stick with respect to the LDC's, and that is really what you are referring to, Senator Mattingly. We really have not attached much of a cost to LDC's or anybody else for staying outside of the GATT. Nor have we attached much of a cost to what LDC's do to harm the United States either in or out of the GATT. It seems to me it would be very healthy for the United States to begin to attach a cost in some of those cases. You might find more countries joining the GATT if they discovered that there was a price to be paid for staying out.

The second point I want to make goes back early on the comment about adjustment assistance. I do not disagree with my colleagues that adjustment assistance is important, but I would simply say that it is a lot more complicated than the commentary thus far would indicate.

We had a difficult time with adjustment assistance programs in the 1970's. They did not work well at all. We poured a lot of money down the rathole. A lot of those funds went to people who did not adjust at all. Therefore, if we are going to have adjustment assistance become a part of our trade policy picture, a significant part, we would better figure out how to do it right. We surely have not figured that out yet!

Senator MATTINGLY. Roth-Kemp was the best yet.

Senator ROTH. Thank you. I think you raise a valid point and I certainly concur.

Both the last administration and this administration was not happy with what we had and I think probably with some justification, but I do think that there is some need to have some kind of a program. Assistance should be more timely and really get to those we are trying to help, and I go back to a point I raised earlier that if we are going to do it that that is a legitimate burden for the trading system to bear the cost by allowing some kind of a tax for that purpose.

I think Mr. Hormats has to leave. We can go on just a few minutes more. I would just like to make a couple observations.

One thing I don't think we have pointed out is that probably some of the problems we have been experiencing with GATT are because of the world economy. I mean, this is a period of time when every country, for political and other reasons, is going through a very hard adjustment. But perhaps now that we are beginning to emerge from that crisis—as you have said—this is a time to look forward to get that momentum moving again.

The one thing I guess or the question that I would like to raise is, How do we get the underdeveloped and the Third World countries more involved in the process? We have touched on this. Bob, I think you have to go.

Mr. HORMATS. Just one thought on that. I think we have got to do this because developing countries are a growing force in the trading and financial system. The problem with negotiations with the developing countries is that some of them do not feel comfortable in selective groups. In the past at least, there was a great deal of feeling that you had to have a lot of developing countries in the

meetings because none of them wanted to take on the burden of representing their colleagues. The natural thing would be to have the Mexicos, Brazils, Argentinas, Indias, and Pakistans be the main negotiators, but they do not want the burden or responsibility of representing the others. Yet, at some point, we are going to have to be selective and the key developing country trading nations will need to participate. They need to get into the process fairly early on, and others can follow.

I think the best way to do this initially is through very low-key, quiet consultations and then begin to identify where we want to go, what sorts of things we can do together and can get out of the negotiations, and what we are all willing to put in. They have to put in something if they want the legitimacy of the bargaining table.

I know Bill Brock is trying to pull together a group of the major trade ministers of the major developed and developed countries and I think that is an excellent place to start, and ultimately the best thing to do is to have these discussions proceed very quietly, very low key, and try to develop a consensus as to where they can give and what they want to get and push it along from there. There are no easy answers to this issue.

There is one factor at play at the current moment. That is that the developing countries' imports are constrained not by their tariff barriers or their quotas, but by the fact that they do not have financing for imports and they do not have very much in the way of foreign exchange to spend. So in one sense, this is not a bad time for developing countries to liberalize because it will not mean a gush of imports into these countries because the imports, as I said, are constrained by financial factors. It is a good time for them to do it. So that as the health of their economies improve and as their foreign exchange orders increase, they will also gradually begin to be able to absorb more imports. In other words, they will be able to adjust by increasing imports as their economies and their financial conditions also improve.

It is not a bad time from the adjustment perspective for them to make these commitments and I think it would also give them credibility at the bargaining table in asking for industrialized countries to improve their procedures as well.

Senator ROTH. Thank you, Bob.

Mr. BERGSTEN. I just wanted to make one comment on your question about how to do trade adjustment and Mr. Yeutter's comment that administrations of all varieties have been unhappy with the nature of the program, even when recognizing the need for such a program.

I do not pretend to have all the answers, but I would want to mention that my Institute for International Economics is now about halfway through a major study of the problem. We are looking at all the various labor adjustment efforts that have been made in this country over the past 20 or 30 years. We are looking at the experience of a dozen foreign countries to see if we can learn from them what might work here and see if out of the record of the past, plus ideas of how one might promote particularly the labor side of the adjustment problem, we might fashion a more effective program.

Included in that is some thinking about the financing techniques, and there the notion mentioned earlier of using tariff revenues may have some potential. In fact, what you could even do is convert existing nontariff barriers over to their tariff equivalents, use at least part of those revenues to finance adjustment, phase down through a negotiation with the other trading partners those tariff barriers that are part of the adjustment of the industry.

So you start with higher levels of barriers that generate funds to adjust out of the industry. As the adjustment progressed, the barriers come down and you need less money. It fits together very neatly.

We are trying to work out in the context of specific industry problems, making estimates of how much is needed, how the money might be used, and would hope to have by the end of this year or early next year a program that we could suggest to the administration and to the Congress. You could hold hearings on that next year to see whether perhaps one could fashion a new approach, because I would fully agree that the need is clear but the way to carry it out, at least at the moment, is not.

Senator ROTH. I strongly endorse that.

Mr. PATTERSON. I have two very short comments, Senator. One is on the charges on imports to finance adjustment. That is a very good idea, but I think what is important to appreciate is that you have to be careful about the words "special charges." That is, if the charges are additional, either to the current tariffs or the tariff equivalent of nontariff measures, then you would be in deep trouble almost immediately because that would be regarded as an additional import constraint and a violation of all of your obligations.

Mr. BERGSTEN. Not if all countries did it together.

Mr. PATTERSON. No; not if all countries did it together.

Mr. BERGSTEN. That was the idea.

Senator ROTH. The suggestion I made earlier was that perhaps this is a matter that ought to be taken up in any negotiations, that somehow there be some kind of a fee—tariff or whatever you want to call it—permitted for the express purpose of providing some kind of adjustment. I think you can argue that that is a burden that trade should shoulder.

Then Mr. Hormats made the point that already under the Trade Act of 1974 it was his understanding that tariff funds were to be used for such purposes, as I recall.

Mr. PATTERSON. The other point that Mr. Hormats made just before he left—my own experience indicates that in dealing with the LDC's, especially the advanced ones, the so-called NIC's, that there is no problem in having serious hard discussions with the Indians, the Brazilians, the Mexicans, the advanced Koreans, provided it is made clear that they are not talking for all LDC's. Once you say, "Well, we are going to talk about an LDC problem," then all the other countries out there will not let them talk. But if you are talking about the particular problems about which you expect these countries to do something and you are not asking others, then I think one finds that many of these countries have very competent and very good and serious negotiators.

Mr. BERGSTEN. One other aspect of that gets to the differences within LDC governments. You will frequently find the Foreign

Ministry of an advanced developing country unwilling to violate his ties with his colleagues in the Group of 77. The Finance and Economics Minister in that same government are very happy to talk pragmatically about how to get on with the business. So you have to be talking to the right people within a country as well as with the right country.

Mr. YEUTTER. I was going to make essentially that same point in a little different way by saying that it seems to me what we need to do in GATT, Mr. Chairman, is to get those key advanced LDC's in, however, we have to go about doing it. We ought to go one by one and convince them to totally immerse themselves in the process of the next round. In the last round they were primarily takers and not very much in the way of givers, and it seems to me that they need to play a much more active role and a role that is a lot more comparable to that of the developed countries.

My other point would be that the timing is propitious because with the debt problems that many of them have they need market access. So there is considerable leverage in bringing them in.

One final point goes back to Mr. Patterson's earlier comment about GATT panels and how much they delay the process. Is it not ludicrous that with all the panels we have with a variety of legal formats in this world—we use arbitration panels and every other type of panel in the United States—it takes forever to put a GATT panel together. There really is not any excuse for that.

Obviously, the reason it takes so long is because the countries that are involved in the dispute want to pack the panels. But there has to be a way to overcome that. Again, that is just a question of commitment on the part of the major nations to have the system work, and at the moment at least there is insufficient commitment to make the panel or dispute settlement process work properly. None of the members of the GATT deserves any gold stars for the way that system fails to function. It is their own darned fault.

Senator ROTH. Well, it is a little after 12. I want to thank all of you for coming here and participating today. I would hope that you feel this discussion has been as fruitful as I do and, frankly, we intend to continue and come back and call you more.

I just might summarize two or three points because I think they are worth reviewing.

I think there is general agreement that we ought to move aggressively in the trade area, that the concepts of equitable and expanding trade are appropriate principles today, that the time is ripe to begin to lay the groundwork for new trade negotiations and that the London Summit would be a fine situation to initiate such action. I think most of you seem to feel that to the extent that we can support equitable and expanding trade by reform of the GATT system that that is the way to go. With at least one dissent, bilateral and other agreements, as long as they are in the direction of expanding trade, are seen to be useful. Finally, we all agree strongly that the future welfare, jobs and health of this country depend upon trade expansion and not protectionism.

Gentlemen, thank you very much. I really appreciate your taking the time to be here today.

The subcommittee is adjourned.

[Whereupon, at 12:10 p.m., the subcommittee adjourned, subject to the call of the Chair.]

[The following information was subsequently supplied for the record:]

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May 30, 1984

The Honorable William V. Roth, Jr.
Chairman Joint Economic Subcommittee
on Trade Productivity and Economic Growth
104 Hart Building
2nd and C Streets, N.E.
Washington, D. C. 20510

Dear Senator Roth:

I want to thank the Committee for the opportunity to prepare written testimony concerning U.S. policy toward the "international trading system." During the last several years, the United States international competitiveness has deteriorated due to several factors. The international position of the U.S. chemical industry, traditionally a strong exporter, has also declined throughout this period. Between 1981 and 1983, chemical exports of several major U.S. chemical companies declined by approximately 13%.

Chemical Companies - Exports and Transfers from the United States
1981-83 (Dollars in Millions)

	1983	1982	1981
Air Products & Chemicals	$79.3	$90.8	$138.7
American Cyanamid	272.8	275.8	261.5
Celanese	490.0	494.0	665.0
Dow Chemical	824.0	826.0	924.0
Du Pont (a)	3,573.0	3,740.0	3,868.0
Herculese	245.0	278.0	335.0
Monsanto	879.0	864.0	1,042.0
Raychem	72.6	83.8	60.2
Rohm and Haas	208.9	203.0	230.2
Stauffer	74.3(b)	108.8	129.4
Union Carbide	926.0	979.0	1,090.0
Total	$7,644.9	$7,943.2	$8,744.0

(a) Primarily from chemical operations; there are only modest coal and refined products exports.
(b) Reflects only nine months' sales, because a September 30 fiscal year was adopted in 1983.

One of the reasons for this decline in U.S. exports can be traced to problems that have occurred in the international trading system. For instance, several of our principal trading partners have made foreign trade central to their development strategies. These countries protect their domestic manufacturing markets and promote their exports -- particularly to the large U.S. market.

While our government has granted some protection to our industries, several countries have assisted (through industrial targeting) their industries to expand their share of world trade. These countries have also placed effective tariff and/or non-tariff barriers on their markets.

Last year, the U.S. trade deficits with Japan and Taiwan, for example, amounted to almost $30 billion -- approximately 50% of the U.S. total trade deficit. This deficit could be reduced if the U.S. would take strong steps to open up these foreign markets to American goods while minimizing the impact of industrial targeting on American industries. Although Japanese tariffs are low, there are a number of non-tariff barriers which effectively keep out U.S. and other foreign products (see Japanese Barriers to U.S. Trade and Recent Japanese Government Trade Initiatives; Office of the United States Trade Representative, November 1982.)

While the United States should continue to engage in multilateral negotiations to open up markets, our government must also continue to pursue "bilateral" efforts to improve the trade environment with our key trading partners. The "High Technology Agreement" and the recent beef and citrus agreements were designed to increase U.S. exports to Japan. But, these measures may not have gone far enough as indicated by the growing trade deficit between the U.S. and Japan. In an effort to reduce the deficit, delegates from the Japan-U.S. Businessmen's Conference stated: "The two sides (both U.S. and Japanese businessmen) agreed to support government efforts to identify American sources that meet Japanese market requirements while encouraging Japanese procurement officials to purchase these products." (Joint Communique -- 20th Japan-U.S. Businessmen's Conference -- July 1983.)

In addition to providing a framework for supporting U.S. exports and imports, bilateral treaties can contribute to: 1) improved protection of U.S. property rights, 2) reduction or elimination of tariffs, non-tariff barriers, and other trade distorting factors, and 3) an adequate safeguard system.

- Intellectual Property Rights Protection-Patents: A strong patent system facilitates technological development in the United States and abroad. Patent protection provides both incentives for invention and innovation within the U.S. as well as incentives for movement of technology between nations. American companies need strong patent protection to recoup R&D costs and to earn a reasonable rate of return on investment. Poor patent protection discourages risk taking and undercuts the international competitiveness of U.S. high technology industries.

- Tariffs, Non-Tariff Barriers, and Trade Distortions: All agreements should address tariffs, non-tariff barriers and trade distorting factors such as subsidies. For example, some countries, with strong external accounts, place outright bans on imports on certain products from the U.S.

while they enjoy a substantial trade surplus with the United States. Other countries require large deposits on imports or a rigorous licensing procedure to import a product. These issues have to be settled to the mutual satisfaction of the U.S. and the other countries if world trade is to continue to expand.

- Safeguards: A more equitable safeguard system should be developed -- possibly modeled on the effective process established in the GSP legislation. At the recent GATT Ministerial Conference, last November, U.S. efforts to open discussions on defining a safeguard system were not well-received. The safeguard system should provide the mechanism to allow U.S. manufacturers an opportunity to adjust to new market forces. In the past, the U.S. has had to negotiate special orderly market agreements (for example, textiles and autos) that have taken into consideration the consumer and the U.S. and foreign manufacturers.

In general, Monsanto strongly supports our government's efforts to strengthen U.S. international economic relations through bilateral and multilateral trade treaties. However, in these discussions our government should also make a distinction between the advanced developing and developed countries with a strong current account position (such as Taiwan and Japan) and those with severe balance of payments problems (such as Brazil, Mexico, and Argentina). In this regard, the United States should be willing to grant a "realistic" amount of time to obtain a phased-in reduction of tariff, non-tariff barriers, and export incentives with those countries with weak economies -- without sacrificing import safeguards or protection of U.S. intellectual property rights.

In addition, we hope U.S. industry representation can continue to play a role in these bilateral negotiations. U.S. industry has a lot riding on these negotiations and our knowledge of the markets and products would be an asset in these discussions.

Finally a few words are necessary on the overvalued dollar and the high cost of capital in the U.S. compared to our trading partners. The U.S. has followed a tight monetary policy while our principal trading partners have emphasized fiscal restraint. As a result of these policy differences, the U.S. has had a higher cost of capital, an overvalued dollar, and a loss of international competitiveness. These macro-economic factors have also contributed to a loss of competitiveness in the U.S. chemical industry, despite the successful effort by the chemical industry to lower its break-even costs significantly. In the future the U.S. needs to coordinate more effectively our economic policies with our trading partners. I hope these remarks prove useful in your discussions and I would be glad to continue this dialogue with the Committee in the future.

Yours truly,

T. L. Gossage

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